STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on April 25, 2001

COMMISSIONERS PRESENT:

Maureen O. Helmer, Chairman
Thomas J. Dunleavy
James D. Bennett
Leonard A. Weiss
Neal N. Galvin

CASE 00-C-1415 – Joint Petition of Global Crossing Ltd. and Citizens Communications Company for approval of the transfer of capital stock of their New York ILECs (Frontier of Rochester, AuSable Valley, New York, Sylvan Lake, and Seneca-Gorham) and Frontier Subsidiary Telco, Inc. to Citizens Communications Company, and for Other Authorization Needed.

ORDER APPROVING TRANSACTION WITH CONDITIONS

(Issued and Effective May 11, 2001)

BY THE COMMISSION:

THE PETITION

On August 22, 2000 Global Crossing Ltd., Global Crossing North America, Inc. and Citizens Communications Company petitioned the Commission for approval to transfer the capital stock of the Frontier New York local exchange companies, including Frontier Telephone of Rochester (FTR), Frontier Communications of Rochester, of AuSable Valley, of New York (the former Highland Telephone Company), of Sylvan Lake and of Seneca-Gorham, and Frontier Subsidiary Telco to Citizens Communications Company.

On July 11, 2000, Global Crossing Ltd., Global Crossing North America (formerly Frontier Corporation) and

Citizens executed an Agreement whereby Citizens would purchase the stock of the five Global Crossing (formerly Frontier) local exchange companies in New York, as well as Frontier Communications of Rochester, Inc., a competitive local exchange company providing service in the Rochester area. In addition, Citizens will acquire Frontier Subsidiary Telco, Inc. (which operates the Frontier companies outside New York), and its subsidiary, Frontier Communications of America, Inc., which will provide long distance service to the existing Global Crossing long distance customer base. The practical effect is that Citizens will become the owner of the group of telephone companies, both within and outside New York State, which are currently owned and operated by Global Crossing North America.

Petitioners claim that no material changes are proposed, nor expected to result, from the proposed transaction. According to the petition, Citizens is paying Global Crossing approximately $3.65 billion[1] (which equates to $3,400 per access line) for the common stock of these phone companies. This purchase price is approximately $2.75 billion over Global Crossing's book value.

Under Section 100 of the Public Service Law, the purchaser of stock of a telephone corporation (here Citizens Communications) has the burden of showing that such a sale is in the public interest. Under Section 99(2) Commission approval is required where a carrier’s franchise is affected. The broad public interest standard, which provides the Commission wide discretion, is used to evaluate both section 100 and 99(2) transactions. Therefore, petitioners seeking approval of

[1] An April 26, 2001, press release from Global Crossing states that the price has been reduced to $3.5 billion.

acquisitions and/or mergers are required to demonstrate that the proposed transaction will meet the public interest standard.

Petitioners claim that the instant transaction is in the public interest and will be transparent to customers in terms of rates, customer service and service quality. In addition, Petitioners claim that there are benefits that will accrue to consumers as a result of this transaction. For example, Citizens' experience with largely rural and suburban communities will allow the combined entities to bring a "sharper focus" to such areas, and the size and expertise of the combined operation will enhance the ability to bring new and innovative services to an "underserved market".

Petitioners also claim that the transaction will increase the availability of enhanced services such as Digital Subscriber Lines. Finally, the Petitioners claim the combined entity can be expected to grow operations beyond the current size of their separate operations thereby increasing the ability to "focus on growing their customer base through new business opportunities, both inside and outside the Citizens and Frontier ILEC territories".

COMMENTS

On September 13, 2000, a Notice Requesting Comment was issued for this case. Initial comments were received from six parties: AT&T, Choice One, the State Consumer Protection Board (CPB), the Communications Workers of America (CWA), Fiber Technologies and the Public Utilities Law Project of New York (PULP). WorldCom, Inc. filed a letter in support of AT&T's Initial Comments regarding Citizens' intrastate-switched access rates. Reply comments were received from Petitioners as well as Fiber Technologies. Generally, the issues raised were broad in scope and included access charge levels, competitive issues, service quality, and workforce and pension issues, as well as, retention of assets, workforce, headquarters and operations in New York. In reaching our determination, we have considered all the proposals addressed in the comments. Some of the issues are also being considered in other, ongoing Commission proceedings.

DISCUSSION

In general, the Commission seeks to ensure just and reasonable rates, that the petitioners' financial integrity is maintained, that a high level of local service quality is maintained, and that no impediments exist in the development of local exchange competition in the petitioners' market areas. We have long emphasized the importance of competition in the development of a viable regulatory framework for the transitional telecommunications environment. Our review of the proposed transaction indicates that, with the addition of the conditions that we are imposing in this order, the transaction will be in the public interest and warrants approval.

Generally, increased market concentration is associated with decreased competition. The acquisition of Frontier by Citizens results in the second and third largest New York incumbent local exchange operating entities being controlled by the same interest. The acquisition will end existing competitive pressure between Frontier and Citizens, and will remove any associated incentives to provide better service and lower prices to New York customers. The costs associated with this foregone competition must be weighed against the benefits of the efficiency savings that might be obtained if Frontier and Citizens combined their operations in some fashion and shared those improvements with customers.

In light of the decreased competition resulting from the transaction, we will condition our approval on the acceptance of measures to mitigate these effects. In the interest of creating a more expeditious process for competitors, petitioners will be required to create, within one year of closing, a single interconnection agreement template covering competitive access to the more than 1.1 million retail customers served by all of the petitioners' New York ILEC operating companies. Petitioners will also be required to establish, within one year of closing, a wholesale service organization that will assign each CLEC a single wholesale service representative for all Citizens/Frontier New York operations. In addition, a single "Local Service Provider Guide," including information for all Citizens/Frontier New York operating companies, will be made available to CLECs on a single web location, within two years of closing.

The Stock Purchase Agreement submitted with the petition prohibits Global Crossing from competing within 20 miles of the Frontier ILEC service territories for a three-year period. On its face this clause contravenes our stated policy of encouraging competition within the State. Recognizing however, that Global Crossing could use its existing ties to consumers to win back customers during the transition period, we will allow a non-compete clause for a period of one year from the date of closing, solely within Frontier's New York ILEC service territories.

In December 2000, we approved a rate restructuring for Citizens which permitted the company to introduce an equitable rate structure as well as overall rate increases to cover lost EAS subsidy revenues and the elimination of Locality Charges state-wide.[2] We anticipate that the instant transaction will

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[2] Case 00-C-0754, <u>Order Approving Rate Rebalancing Plan</u>, (issued January 9, 2001).

result in substantial savings to the companies from revenue enhancements and administrative savings. In view of the gradual accrual of anticipated transactional savings, the recently-approved overall rate increases are now unnecessary for providing service at just and reasonable rates. Accordingly, the overall rate increases will be eliminated.

Recognizing that such savings will take time to be generated, and in keeping with the originally-authorized Restructure Plan, we will authorize the use of outstanding customer credits to offset the rate decrease. Citizens will be permitted to use $4.9 million of customer credits in 2001 and 2002. In 2003, the customer credits that Citizens will be permitted to use will be reduced to $2.45 million. To enhance Citizens’ efficiency and protect ratepayers, Citizens will not be permitted to file for rate increases to be effective sooner than January 1, 2004.

The basic rate restructuring that we recently approved will be implemented. As a result, some customers’ bills will increase or decrease as rate group uniformity is implemented and locality charges eliminated. However, most resulting increases will be significantly less with the elimination of the $4.9 million revenue increase. Within 60 days of the closing of the transaction, petitioners will be required to file a revised Restructure Plan reflecting the elimination of the scheduled rate increases.

The petitioners will be required to increase the Lifeline discount in the Frontier ILECs other than FTR from $1.75 to $3.50. The existing Lifeline deferral will be eliminated and the accumulated Lifeline deferral will be used to fund the revenue loss. Once the accumulated deferral is exhausted, the companies will absorb the revenue loss indefinitely.

As a result of the Global Crossing/Frontier merger approved by the Commission in September 1999, Frontier’s New York ILEC customers have been insulated from any increase in capital costs resulting from the merger. Citizens has agreed to retain this customer protection for Frontier’s New York companies as well as extend it to the New York customers of Citizens. An “AA-“ and an “A+“ cost of capital will be imputed for Frontier and Citizens ILECs, respectively, if any rate requests are filed, if their respective credit ratings are below these levels. The “AA-“ imputed-rating for Frontier’s New York ILEC companies represents Frontier’s credit rating before the Global Crossing merger took place. The “A+“ credit rating for Citizens’ ILECs represents Citizens’ credit rating before the instant acquisition was announced.

In the examination of Frontier’s New York ILECs’ books in conjunction with this transaction it was discovered that those companies have not complied with the Commission’s Statement of Policy on Pensions and Post Retirement Benefits Other Than Pensions (OPEB)[3]. Frontier has committed to comply with the Policy Statement. Nevertheless, we will require each Frontier ILEC in New York to make a compliance filing with regard to Pensions and OPEBs. All Pension and OPEB calculations, and the corresponding accounting journal entries for each of the Frontier ILEC Companies in New York, must be approved by the Director of the Office of Accounting and Finance.

In its petition in support of the approval of its transaction, Citizens had agreed to abide by all of the commitments made by Global Crossing when it acquired the

[3] Case 91-M-0890, Pensions and Post Retirement Benefits Other Than Pensions, (issued September 7, 1993).

Frontier companies in 1999.[4] Several of these commitments are designed to reduce the risk that managerial and financial resources will be diverted away from the Frontier ratepayers. We will condition our approval on petitioners adherence to the commitments. They include:

1. Initially the Frontier headquarters will remain in Rochester;
2. The existing Frontier management team will remain largely in place;
3. The Frontier name will be retained;
4. Investment in the network and workforce will be maintained at levels that are required, in Petitioners' view, to provide good service quality to both residential and business customers.
5. All books and records will be maintained in New York, or access will be provided in New York. If review is required of out-of-state books or records, the Department of Public Service will be compensated accordingly;
6. All management and craft forces required for the New York operation will be maintained and Citizens will ensure that such forces provide good service quality to consumers;
7. Citizens will insulate Frontier ratepayers[5] from the imposition of any fees, costs, or penalties related to the transaction;

[4] Case 99-C-0530, Joint Petition by Global Crossing, Ltd. and Frontier Corporation for Approval of the Acquisition by Global Crossing, Ltd. of all the Outstanding Shares of Frontier Corporation's Common Stock, (issued December 1, 1999).

[5] In reply comments, the petitioners have agreed to extend these protections to Citizens' ratepayers.

8. Citizens will insulate Frontier ratepayers[6] from any increase in the cost of debt or equity resulting from the transaction.

While we expect Citizens to pursue corporate efficiencies, any such efforts must be done consistent with maintaining an adequate and fair focus on New York's interests. Therefore, we condition our approval such that Citizens shall maintain a major operations and administrative center in New York State to support its New York companies, and shall treat New York workers equitably in terms of employment vis-à-vis the relocation or consolidation of job functions.

Citizens has also agreed to be bound by existing Open Market Plan provisions including the permanent holding company protections which relate to Frontier's financial integrity and service quality, limitations on affiliate transactions[7], and rules governing borrowing and cash management. Citizens also agreed to the service quality commitments and penalties contained in the modification of the Plan approved by the Commission in March 2000.[8] In addition to the retail service quality obligations, the Open Market Plan contains a Carrier-to-Carrier Service Quality Performance Incentive that also will remain in place.

We expect that this acquisition will not affect the generally excellent service quality provided by Citizens and the

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[6] Id.

[7] The reasonableness and cost effectiveness of service contract charges between affiliate companies involved in this transaction must be demonstrated in any future rate proceeding.

[8] Case Nos. 93-C-0103 and 93-C-0033, Opinion and Order Establishing New Terms of Open Market Plan and Rate Plan, (issued March 30, 2000).

Frontier ILECs not subject to the conditions of the OMP. To protect this expectation, we will require Citizens and the Frontier subsidiaries other than FTR, to notify the Director of the Office of Communications in any instance where less than 90% of a given company’s central offices are below a CTRR level of 3.3 reports per 100 access lines in any 12–month period ending each calendar quarter. Such notification should include an explanation of why the CTRR criterion was not met and plans for improvement.

CONCLUSION

Based on our review of the petition and the comments thereon, we find that the conditions, commitments and agreements discussed in this order are necessary to offset any detriments to New York consumers and provide them tangible benefits from the transaction. Subject to the conditions, commitments and agreements discussed in this Order, we find that the transaction is in the public interest and will be approved pursuant to Public Service Law, Sections 99 and 100.

The Commission orders:

1. The acquisition of the capital stock of Global Crossing North America, Inc.’s New York local exchange companies (Frontier Telephone of Rochester, Frontier Communications of Rochester, of AuSable Valley, of New York, of Sylvan Lake and of Seneca-Gorham), and Frontier Subsidiary Telco, Inc. by Citizens Communications Company is approved, pursuant to Public Service Law Sections 99 and 100, subject to the conditions, commitments and agreements discussed in this Order. Except where contrary to the provisions of this Order, the acquisition shall be as prescribed in the Stock Purchase Agreement dated July 11, 2000.

2. Citizens Communications Company shall insulate New York ratepayers from the imposition of any fees, costs, or penalties related to the transaction. The excess of purchase price over book value shall neither be charged to New York ratepayers nor included on the books and records of any of the New York ILECs. Citizens Communications Company shall insulate New York ratepayers from any increase in the cost of debt or equity resulting from the transaction.

3. Within 120 days of the closing of the transaction, Citizens Communications Company shall make a compliance filing, demonstrating compliance with the Commission Policy Statement on Pensions and OPEBs (Case 91-M-0890, Pension and Post Retirement Benefits Other Than Pensions, issued and September 7, 1993) for Frontier Telephone of Rochester. Within 30 days of the closing of the transaction, Citizens Communications Company shall make a compliance filing for all the other Frontier ILECs, demonstrating compliance with the Commission Policy Statement on Pensions and OPEBs. All pension and OPEB calculations, and the corresponding accounting journal entries for each of the Frontier ILEC Companies in New York, must be approved by the Director of the Office of Accounting and Finance.

4. Within 30 days of posting the final closing journal entries for this transaction, Citizens Communications Company shall file with the Director of the Office of Accounting and Finance, a copy of all of the accounting journal entries related to this transaction for all the New York ILEC companies and their parent company, Citizens Communications Company.

5. Within one year of the closing of the transaction, Citizens Communications Company shall create a single interconnection agreement template covering access to all its ILEC customers in New York State.

6. Within one year of the closing of the transaction, Citizens Communications Company shall establish a wholesale service organization that will assign each CLEC a single wholesale service representative for all Citizens Communications Company's New York ILEC operations.

7. Within two years of the closing of the transaction, Citizens Communications Company shall make available to the CLECs on a single web location, a single "Local Service Provider Guide" including information for all its New York ILECs.

8. The terms of the Stock Purchase Agreement that prohibit Global Crossing from competing in and around Frontier's service territory shall be limited to one year from the closing of the transaction, and shall apply solely within Frontier's New York ILEC service territories.

9. The petitioners shall increase the Lifeline discount in the rates of the Frontier ILECs other than Frontier Telephone of Rochester, from $1.75 to $3.50. The existing deferral shall be eliminated and the accumulated deferral shall be used to fund the revenue loss. Once the accumulated deferral is exhausted, the companies shall absorb the revenue loss.

. 10. Citizens Communications Company and the Frontier subsidiaries other than Frontier Telephone of Rochester, shall be required to notify the Director of the Office of Communications in any instance where less than 90% of a given company's New York central offices are below a CTRR level of 3.3 reports per 100 access lines in any 12-month period ending each calendar quarter. Such notification should include an explanation why the CTRR criterion was not met and plans for improvement.

.   11. Citizens Communications Company shall file tariffs within 60 days of the closing of the transaction, reducing its rates by $4.9 million dollars to become effective 30 days later. Citizens Communications Company will be permitted to use $4.9 million in customer credits in each of 2001 and 2002, and $2.45 million in 2003. Citizens Communications Company shall not file for rate increases to be effective prior to January 1, 2004.

12. Within 60 days of the closing of the transaction, Citizens Communications Company shall file a revised Restructure Plan that reflects the rate reduction from paragraph 11.

13. The Commission shall have unrestricted access to the books and records of Citizens Communications, Inc. and its affiliates with respect to transactions by and among affiliates and between affiliates and third parties. The books and records of the New York ILEC companies shall not be removed from New York State unless permission is granted by the Commission. If review is required of out-of-state books or records, the Department of Public Service will be compensated accordingly.

14. This order shall be without force and effect until there has been filed with the Commission an unconditional written acceptance by the petitioners agreeing to obey all the terms and conditions of this order. If such acceptance is not filed within a period of ten (10) days from the date of this order, this order may be revoked by the Commission without further notice.

15. The parties to this transaction shall notify the Commission within 30 days of its completion that this approved transaction has taken place. If the authority granted by this order is not exercised within one year of the effective date of this order, the order may be revoked by the Commission without further notice

. 16. This proceeding is continued.

By the Commission,

(SIGNED) JANET HAND DEIXLER
Secretary