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FROM: Ernest G. Johnson
Director
Utilities Division

DATE: August 2, 2002

RE: IN THE MATTER OF THE APPLICATIONS OF THE ACSI LOCAL SWITCHED SERVICES, INC. DBA E.SPIRE AND AMERICAN COMMUNICATION SERVICES OF PIMA COUNTY, INC. DBA E.SPIRE AND XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES LLC AND XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, L.L.C. FOR EXPEDITED APPROVAL OF (I) THE TRANSFER OF SUBSTANTIALLY ALL OF THE ASSETS, INCLUDING THE CUSTOMERS CONTRACTS, OF THE E.SPIRE OPERATING ENTITIES TO THE XSPEDIUS OPERATING ENTITIES; (II) THE DISCONTINUANCE OF THE TELECOMMUNICATIONS SERVICES IN ARIZONA BY THE E.SPIRE OPERATING ENTITIES, ALSO IN THE MATTER OF THE APPLICATIONS OF THE XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, LLC AND XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES, LLC FOR A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE INTEREXCHANGE AND LOCAL COMPETITIVE SERVICES AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES WITHIN THE STATE OF ARIZONA (DOCKET NOS. T-04112A-02-0450, T-04113A-02-0450 T-03597A-02-0450, T-03411A-02-0450, T-04112A-02-0451 AND T-04113A-02-0452)

Attached is the Staff Report for the above referenced applications. Besides the transfer of assets from e.Spire Operating Entities to Xspedius Operating Entities, the Xspedius Operating Entities are applying for approval to provide the following services:

- Facilities-based local exchange services
- Facilities-based interexchange services
- Resold local exchange services
- Resold interexchange services

Staff is recommending approval of the transfer of assets and the applications for a Certificate of Convenience and Necessity following a hearing. The discontinuance of

telecommunications service by the e.Spire Operating Entities will be addressed at a later date.

/jfb

Originator: John Bostwick

Attachment: Original and Ten Copies

STAFF REPORT

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

ACSI LOCAL SWITCHED SERVICES, INC. DBA ESPIRE, AMERICAN COMMUNICATION SERVICES OF PIMA COUNTY, INC. DBA E.SPIRE, XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES, LLC, AND XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, LLC

DOCKET NOS. T-04112A-02-0450, T-04113A-02-0450, T-03597A-02-0450, T-03411A-02-0450, T-04112A-02-0451 AND T-04113A-02-0452

IN THE MATTER OF THE APPLICATIONS OF THE ACSI LOCAL SWITCHED SERVICES, INC. DBA E.SPIRE AND AMERICAN COMMUNICATION SERVICES OF PIMA COUNTY, INC. DBA E.SPIRE AND XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES LLC AND XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, L.L.C. FOR EXPEDITED APPROVAL OF (I) THE TRANSFER OF SUBSTANTIALLY ALL OF THE ASSETS, INCLUDING THE CUSTOMERS CONTRACTS, OF THE E.SPIRE OPERATING ENTITIES TO THE XSPEDIUS OPERATING ENTITIES; (II) THE DISCONTINUANCE OF THE TELECOMMUNICATIONS SERVICES IN ARIZONA BY THE E.SPIRE OPERATING ENTITIES, ALSO IN THE MATTER OF THE APPLICATIONS OF THE XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, LLC AND XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES, LLC FOR A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE INTEREXCHANGE AND LOCAL COMPETITIVE SERVICES AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES WITHIN THE STATE OF ARIZONA

AUGUST 2, 2002

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STAFF ACKNOWLEDGMENT

The Staff Report for the applications of the Certificate of Convenience ("CC&N") and Necessity for Xspedius Management Co. of Pima County, LLC and Xspedius Management Co. Switched Services, LLC, petition for a determination that its proposed services should be classified as competitive, transfer of assets from e.Spire Operating Entities to Xspedius Operating Entities, and the discontinuance of telecommunications services by the e.Spire Operating Entities was the responsibility of the Staff member listed below, Docket Nos. T-04112A-02-0450, T-04113A-02-0450, T-03597A-02-0450, T-03411A-02-0450, T-04112A-02-0451 and T-04113A-02-0452. John F. Bostwick was responsible for the review and analysis of applications for a CC&N to provide facilities-based and resold interexchange services and local exchange services; of petitions for a determination that the proposed services should be classified as competitive, the transfer of assets, and the discontinuance of telecommunications services.

John F. Bostwick

John F. Bostwick
Administrative Services Officer II

1. INTRODUCTION

On June 18, 2002, American Communication Service of Pima County, Inc. dba e.Spire ("ACSI Pima") and ACSI Local Switched Services, Inc. dba e.Spire ("ACSI Switched") (the "e.Spire Operating Entities) (collectively, "Petitioners"); and Xspedius Management Co. of Pima, LLC ("Xspedius Pima") and Xspedius Management Co. Switched Services, LLC ("Xspedius Switched") (the "Xspedius Operating Entities") (collectively, "Applicants") filed with the Arizona Corporation Commission ("Commission") an application for authority pursuant to A.R.S. § 40-285 to transfer substantially all the assets of the e.Spire Operating Entities to the Xspedius Operating Entities. The transfer of assets, which represents a "Joint Application", will allow the Xspedius Operating Entities to provide service to the customers of the e.Spire Operating Entities without interruption of service. The Joint Application also requests authority for the e.Spire Operating Entities to discontinue the provision of local exchange service, pursuant to Arizona Administrative Code ("AAC") R14-2-1107. The discontinuance of telecommunications services in Arizona by the e.Spire Operating Entities will be addressed at a later date. The Joint Application arises out of the voluntary petition for Chapter 11 protection that the e.Spire Operating Entities filed with the United States Bankruptcy Court for Delaware (the "Bankruptcy Court") on March 22, 2001. The proposed transaction, Sales Order, was approved by the Bankruptcy Court on June 5, 2002.

Also on June 18, 2002, Xspedius Management Co. of Pima County, LLC and Xspedius Management Co. Switched Services, LLC filed applications for a Certificate of Convenience and Necessity ("CC&N") to provide facilities-based and resold interexchange services and local exchange services within the State of Arizona. The Applicants petitioned the Arizona Corporation Commission for a determination that its proposed services should be classified as competitive.

The Petitioners request expedited treatment and consideration of the Petition because the e.Spire Operating Entities' customers currently are continuing to receive service from ACSI Pima and ACSI Switched. The e.Spire Operating Entities are operating in Chapter 7. If the e.Spire Operating Entities are forced to convert, ACSI Pima and ACSI Switched could shut down and customers not already migrated to the Xspedius Operating Entities could lose service. In order to prevent an interruption of service, the Petitioners request that the Commission grant all relief sought in its Petition as soon as possible.

Staff's review of the applications address the overall fitness of the Applicants to receive a CC&N. Staff's analysis also considers whether the Applicants' services should be classified as competitive and if the Applicants' initial rates are just and reasonable. In addition, Staff reviewed the Petition to ensure the transfer of e.Spire Operating Entities' assets to Xspedius Operating Entities are in the public interest.

2. THE APPLICANTS' APPLICATION FOR A CERTIFICATE OF CONVENIENCE & NECESSITY

This section of the Staff Report contains descriptions of the geographic market to be served by the Applicants, the requested services, and the Applicants' technical and financial capability to provide the requested services. In addition, this section contains the Staff evaluation of the Applicants' proposed rates and charges and Staff's recommendation thereon.

2.1 DESCRIPTION OF THE GEOGRAPHIC MARKET TO BE SERVED

The Applicants seeks authority to provide telecommunications services throughout the State of Arizona.

2.2 DESCRIPTION OF REQUESTED SERVICES

The Applicants propose to provide facilities-based and resold interexchange services and local exchange services. These services include, but are not limited to the following: directory listings and directory assistance, E911 service, CLASS services, and telephone relay service.

2.3 THE ORGANIZATION

The Applicants are a limited liability company organized in the State of Delaware and have authority to transact business in Arizona.

2.4 TECHNICAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

The Applicants will employ seven key employees that have over 90 years of experience in the telecommunications service industry.

2.5 FINANCIAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

The Applicants did provide pro forma financial statements. For the period ending June 1, 2002, the financial statements list Xspedius Switched's assets at $2.3 milliona and Xspedius Pima's assets at $13.6 million. The equity of the Parent Company, Xspedius Management Co, LLC, is projected at $75 million. For the year ending June 30, 2003, Xspedius Switched's net income is projected to be $1.3 million and Xspedius Pima's net income is projected to be $412,943. The Applicants did not provide notes related to the financial statements. Also, the Applicants did state in its Applications that it will rely on its ultimate Parent Company, Xspedius Management Co., LLC, for financial support.

The Applicants stated in its Tariff, Section 2.5.3(s) on pages 36-38, that it collects from its customers an advance, deposit and/or prepayments. Staff believes that an advance, deposit, and/or prepayment received from the Applicants' resold interexchange customers should be protected by the procurement of a performance bond. Since the

Applicants are requesting a CC&N for more than one kind of service, the amount of a performance bond for multiple services is an aggregate of the minimum bond amount for each type of telecommunications services requested by the Applicants. The amount of bond coverage needed for each service is as follows: resold interexchange $10,000 for advances, deposits and/or prepayments collected; resold local exchange $25,000; facilities-based long distance $100,000; and facilities-based local exchange $100,000. The bond coverage needs to increase in increments equal to 50 percent of the total minimum bond amount when the total amount of the advances, deposits, and prepayments is within 10 percent of the total minimum bond amount. Further, measures should be taken to ensure that the Applicants will not discontinue service to its local exchange customers without first complying with AAC R14-2-1107.

To that end, Staff recommends that each Applicant procure a performance bond equal to $235,000. The minimum bond amount of $235,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The bond amount should be increased in increments of $117,500. This increase should occur when the total amount of the advances, deposits, and prepayments is within $23,500 of the bond amount. If either Applicant desires to discontinue local exchange service, it must file an application with the Commission pursuant to AAC R14-2-1107. Additionally, the Applicant must notify each of its local exchange customers and the Commission 60 days prior to filing an application to discontinue service. Failure to meet this requirement should result in forfeiture of the Applicant's performance bond. Staff further recommends that proof of the above mentioned performance bond be docketed within 365 days of the effective date of an Order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission.

However, if at some time in the future, either Applicant does not collect from its customers an advance, deposit, and/or prepayment, Staff recommends that the Applicant be allowed to file a request for cancellation of its established performance bond regarding its resold interexchange service. Such request should be filed with the Commission for Staff review. Upon receipt of such filing and after Staff review, Staff will forward its recommendation to the Commission.

If the Applicants experience financial difficulty, there should be minimal impact to its customers because there are many companies that provide resold telecommunications services or the customers may choose a facilities-based provider. If the customer wants interexchange service from a different provider immediately, that customer is able to dial a 101XXXX access code. In addition, the Applicants' customers could obtain local exchange services from many other carriers certificated to provide such services. In the longer term, the customer may permanently switch to another company.

2.6 ESTABLISHING RATES AND CHARGES

The Applicants would initially be providing service in areas where an incumbent local exchange carrier ("ILEC"), along with various competitive local exchange carriers ("CLECs") and interexchange carriers are providing telephone service. Therefore, the Applicants would have to compete with those providers in order to obtain subscribers to its services. The Applicants would be a new entrant and would face competition from both an incumbent provider and other competitive providers in offering service to its potential customers. Therefore, the Applicants would generally not be able to exert market power. Thus, the competitive process should result in rates that are just and reasonable.

Both an initial rate (the actual rate to be charged) and a maximum rate must be listed for each competitive service offered, provided that the rate for the service is not less than the Company's total service long-run incremental cost of providing the service pursuant to AAC R14-2-1109.

Staff obtained information from the Applicants regarding its fair value rate base. Xspedius Switched reported its fair value rate base to be approximately $2.3 million. Xspedius Pima reported its fair value rate base to be approximately $13.6 million. However, the rate to be ultimately charged by the Applicants will be heavily influenced by the market. Because of the nature of the competitive market and other factors, a fair value analysis is not necessarily representative of the Applicants' operations. Therefore, while Staff considered the fair value rate base information submitted by the Applicants, it did not accord that information substantial weight in its analysis of this matter.

The Applicants lack the market power to adversely affect the interexchange telecommunications market by either restricting output or raising prices. Also, Staff has recommended that the Applicants' services be classified as competitive and thus subject to the flexible pricing authority allowed by the Commission's Competitive Telecommunications Services rules. These two factors, lack of market power and the competitive marketplace for the services the Applicants proposed to offer, support the conclusion that a fair value analysis is not necessarily representative of the Applicants' operations, and that the rates charged by the Applicants will be reasonable.

3. LOCAL EXCHANGE CARRIER SPECIFIC ISSUES

Since the Applicants intend to provide local exchange service, the issues related to the provision of that service are discussed below.

3.1 DIRECTORY LISTINGS AND DIRECTORY ASSISTANCE

Callers should be able to determine the telephone numbers belonging to customers of alternative local exchange companies, such as the Applicants. Staff recommends that the Applicants file a plan, within 365 days of the effective date of the Order in this matter or 30 days prior to the provision of service, whichever comes first,

and must remain in effect until further order of the Commission, how it plans to have its customers' telephone numbers included in the incumbent's Directories and Directory Assistance databases before it begins providing local exchange service.

3.2 NUMBER PORTABILITY

Another issue associated with the Applicants' proposal to become a competitive local exchange company relates to how telephone numbers should be administered. Local exchange competition may not be vigorous if customers, especially business customers, must change their telephone numbers to take advantage of a competitive local exchange carrier's service offerings. Staff recommends that the Applicants pursue permanent number portability arrangements with other local exchange carriers ("LECs") that are consistent with federal laws, federal rules and state rules.

3.3 PROVISION OF BASIC TELEPHONE SERVICE AND UNIVERSAL SERVICE

The Commission has adopted rules to address maintenance of universal telephone service during and after the transition to a competitive telecommunications services market. The rules contain the terms and conditions for contributions to and support received from telephone service subscribers to finance the Arizona Universal Service Fund ("AUSF"). Under the rules, the Applicants will be required to participate in the financing of the AUSF and it may be eligible for AUSF support. Therefore, Staff recommends that approval of the Applicants' application for a CC&N be conditioned upon the Applicants' agreement to abide by and participate in the AUSF mechanism established by Decision No. 59623, dated April 24, 1996 (Docket No. RT-00000E-95-0498).

3.4 QUALITY OF SERVICE

Staff believes that the Applicants should be ordered to abide by the quality of service standards that were approved by the Commission for Qwest (f/k/a USWC) in Docket No. T-01051B-93-0183 (Decision No. 59421). Because the penalties that were developed in this docket were initiated only because Qwest's level of service was not satisfactory, Staff does not recommend that those penalties apply to the Applicants. In the competitive market that the Applicants wish to enter, the Applicants generally will have no market power and will be forced to provide a satisfactory level of service or risk losing its customers. Therefore, Staff believes that it is unnecessary to subject the Applicants to those penalties at this time.

3.5 ACCESS TO ALTERNATIVE LOCAL EXCHANGE SERVICE PROVIDERS

Staff expects that there will be new entrant providers of local exchange service who will install the plant necessary to provide telephone service to, for example, a residential subdivision or an industrial park much like existing local exchange companies do today. In those areas where the Applicants install the only local exchange service

facilities, the Applicants will be a monopoly service provider. In the interest of providing competitive alternatives to the Applicants' local exchange service customers, Staff recommends that the Applicants provide customers served in these areas with access to alternative local exchange service providers. In this way, an alternative local exchange service provider may serve a customer if the customer so desires. With this requirement in place, the Applicants will not be able to exert monopoly power over customers who are located in areas where the Applicants is the only provider of facilities to serve the customer. Access to other providers should be provided pursuant to the provisions of the 1996 Telecommunications Act, the rules promulgated thereunder and Commission rules on interconnection and unbundling.

3.6 911 SERVICE

The Applicants have not indicated in its application whether it will provide all customers with 911 and E911 service, where available, or will coordinate with ILECs and emergency service providers to provide the service. Staff believes that the Applicants should be required to work cooperatively with local governments, public safety agencies, telephone companies, the National Emergency Number Association and all other concerned parties to establish a systematic process in the development of a universal emergency telephone number system. Staff recommends that the Applicants be required to certify, through the 911 service provider in the area in which it intends to provide service, that all issues associated with the provision of 911 service have been resolved with the emergency service providers before it begins to provide local exchange service, within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission.

3.7 CUSTOM LOCAL AREA SIGNALING SERVICES

In its decisions related to Qwest's proposal to offer Caller ID and other CLASS features in the State, the Commission addressed a number of issues regarding the appropriateness of offering these services and under what circumstances it would approve the proposals to offer them. The Commission concluded that Caller ID could be offered provided that per call and line blocking, with the capability to toggle between blocking and unblocking the transmission of the telephone number, should be provided as options to which customers could subscribe with no charge. The Commission also approved a Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated, which indicates that the number has been blocked. The Commission further required that Qwest engage in education programs when introducing or providing the service(s).

Staff recommends that the Applicants be required to abide by all the Commission decisions and policies regarding Caller ID and other CLASS services. However, Staff does not believe that it is necessary for the Applicants to engage in the educational program that was ordered for Qwest as long as customers in the areas where the Applicants intend to serve have already been provided with educational material and are

aware that they can have their numbers blocked on each call or at all times with line blocking.

3.8 EQUAL ACCESS FOR INTEREXCHANGE CARRIERS

Although the Applicants did not indicate that its switch will be "fully equal access capable" (i.e. would provide equal access to interexchange companies), the Commission requires local exchange companies to provide 2-Primary Interexchange Carriers ("2-PIC") equal access. 2-PIC equal access allows customers to choose different carriers for interLATA and intraLATA toll service and would allow customers to originate intraLATA calls using the preferred carrier on a 1+ basis. Staff recommends that the Applicants be required to provide 2-PIC equal access.

4. COMPETITIVE SERVICES ANALYSIS

The Applicants have petitioned the Commission for a determination that the services it is seeking to provide should be classified as competitive. The Applicants have not published legal notice of the applications in all counties in which it requests authorization to provide service. The Applicants have not certified that all notification requirements have been completed. Staff's analysis and recommendations are discussed below.

4.1 COMPETITIVE SERVICES ANALYSIS FOR LOCAL EXCHANGE SERVICES

4.1.1 **A description of the general economic conditions that exist, which makes the relevant market for the service one that, is competitive.**

The analysis of the market for local exchange service that the Applicants seek to enter must take into account the fact that there are two local exchange service submarkets. The first is the local exchange service market that consists of locations where ILECs currently provide service. The second local exchange service market consists of locations within ILECs' service territories where ILECs are authorized to provide local exchange service, but where they do not actually provide service.

The local exchange market that the Applicants seek to enter is one in which a number of new CLECs have been authorized to provide local exchange service. Nevertheless, ILECs hold a virtual monopoly in the local exchange service market. At locations where ILECs provide local exchange service, the Applicants will be entering the market as an alternative provider of local exchange service and, as such, the Applicants will have to compete with those companies in order to obtain customers. In areas where ILECs do not serve customers, the Applicants may have to convince developers to allow it to provide service to their developments. Staff recommends that, in those instances where the Applicants provide the only facilities used to provide telecommunications service, that the

Applicants be required to allow other local exchange companies to use those facilities to serve customers who wish to obtain service from an alternative provider pursuant to federal laws, federal rules and state rules.

4.1.2 **The number of alternative providers of the service.**

Qwest and various independent LECs are the primary providers of local exchange service in the State. Several CLECs and local exchange resellers are also providing local exchange service.

4.1.3 **The estimated market share held by each alternative provider of the service.**

Since Qwest and the independent LECs are the primary providers of local exchange service in the State, they have a large share of the market. Since the CLECs and local exchange resellers have only recently been authorized to offer service they have limited market share.

4.1.4 **The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicants, as defined in AAC R14-2-801.**

None.

4.1.5 **The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms and conditions.**

ILECs have the ability to offer the same services that the Applicants have requested in their respective service territories. Similarly many of the CLECs and local exchange resellers also offer substantially similar services.

4.1.6 **Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).**

The local exchange service market is:

a. One in which ILECs own networks that reach nearly every residence and business in their service territories and which provide them with a virtual monopoly over local exchange service. New entrants are also beginning to enter this market.

b. One in which new entrants will be dependent upon ILECs:

1. To terminate traffic to customers.

2. To provide essential local exchange service elements until the entrant's own network has been built.
3. For interconnection.

c. One in which ILECs have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market and one in which new entrants do not have a long history with any customers.

d. One in which Qwest provides a quality of service that has generated a significant number of complaints. These complaints led the Commission to adopt service quality rules that contain penalties if the service quality standards are not met. A provider of alternative service, such as the Applicants, should provide Qwest--as well as other incumbents--with the incentive to produce higher quality service including service installation and repair on a timely basis.

e. One in which most customers have few, if any choices since there is generally only one provider of local exchange service in each service territory.

f. One in which the Applicants will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

4.2 COMPETITIVE SERVICES ANALYSIS FOR INTEREXCHANGE SERVICES

4.2.1 **A description of the general economic conditions that exist, which makes the relevant market for the service one that, is competitive.**

The interexchange market that the Applicants seek to enter is one in which numerous facilities-based and resold interexchange carriers have been authorized to provide service throughout the State. The Applicants will be a new entrant in this market and, as such, will have to compete with those companies in order to obtain customers.

4.2.2 **The number of alternative providers of the service.**

There are a large number of facilities-based and resold interexchange carriers providing both interLATA and intraLATA interexchange service throughout the State. In addition, various ILECs provide intraLATA interexchange service in many areas of the State.

4.2.3 **The estimated market share held by each alternative provider of the service.**

The large facilities-based interexchange carriers (AT&T, Sprint, MCI WorldCom, etc.) hold a majority of the interLATA interexchange market, and the ILECs provide a large portion of the intraLATA interexchange market. Numerous other interexchange carriers have a smaller part of the market and one in which new entrants do not have a long history with any customers.

4.2.4 **The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicants, as defined in AAC R14-2-801.**

None.

4.2.5 **The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms and conditions.**

Both facilities-based and resold interexchange carriers have the ability to offer the same services that the Applicants have requested in their respective service territories. Similarly many of the ILECs offer similar intraLATA toll services.

4.2.6 **Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).**

The interexchange service market is:

a. One with numerous competitors and limited barriers to entry.

b. One in which established interexchange carriers have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market.

c. One in which the Applicants will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

5. TRANSFER OF ASSETS

The e.Spire Operating Entities currently hold a CC&N to provide resold and facilities-based local exchange and interexchange telecommunications services in Arizona. The e.Spire Operating Entities received their CC&N in Decision numbers 60078 and 60711, dated February 19, 1997 and February 27, 1998 respectively.

There are no complaints on file with the Consumer Services Section against the e.Spire Operating Entities. According to the annual reports on file, the e.spire Operating Entities currently provides service to commercial customers in Arizona.

The Xspedius Operating Entities are only interested in acquiring substantially all the assets of the business, including the customer accounts, base, and contracts. The most effective way to acquire those assets from the e.Spire Operating Entities, emerging from bankruptcy, was to transfer those assets to new corporate entities, Xspedius Operating Entities. Any deposits or prepayments collected from e.Spire Operating Entities' customers will be transferred to the Xspedius Operating Entities. Also, to avoid customer confusion, the e.Spire Operating Entities will change their name to match the corresponding name of the Xspedius Operating Entities.

On June 7, 2002, the Petitioners provided thirty (30) days written notice of the proposed transfer to the affected customers of e.Spire Operating Entities. The anticipated date for the transfer of the customers' service is July 8, 2002. According to AAC R14-2-1107, providers of competitive local exchange service, such as e.spires Operating Entities, are required, in part, to furnish: (1) their affected customers with a list of all alternative utilities providing the same or similar service within the affected geographic area; (2) publish legal notice of the application to discontinue local exchange service; and (3) verification that all affected customers have been notified of the proposed discontinuance. In Decision No. 64740, the Commission ordered the local exchange provider to make sure the affected customers receive proper discontinue service notification in full compliance with AAC R14-2-1107, and upon such notice the customers may elect within 90 days (of the Order) to continue or discontinue service in their discretion, without prejudice or regard to contractual obligation.

Staff believes the e.Spire Operating Entities' customers will receive uninterrupted service if this application is approved as requested. Also, Staff feels that the transfer of the assets is in the public interest because: (1) the transfer will eliminate the threat of disruption of service to existing e.Spire Operating Entities' customers who could lose service due to the bankruptcy condition; and (2) increase competition by permitting the Xspedius Operating Entities to re-deployed existing assets to serve existing e.Spire Operating Entities' customers and new customers in a competitive market.

Staff recommends that a hearing be scheduled to approve the transfer of assets as soon as possible due the emergency nature of the application.

Staff further recommends that e.Spire Operating Entities' make sure the affected customers receive proper discontinue service notification in full compliance with AAC R14-2-1107, and upon such notice the customers may elect within 90 days of the Order of this matter to continue or discontinue service in their discretion, without prejudice or regard to contractual obligation.

6. RECOMMENDATIONS

The following sections contain the Staff recommendations on the Applicant's Application for a CC&N, the Applicant's Petition for a Commission Determination that its Proposed Services Should be Classified as Competitive, and the Petitioners' Transfer of Assets.

6.1 RECOMMENDATIONS OF THE APPLICANTS' APPLICATION FOR A CC&N

The Applicants are a limited liability company organized in the State of Delaware and have authority to transact business in Arizona. The Applicants will employ seven key employees that have over 90 years of experience in the telecommunications service industry. The Applicants have demonstrated that they have the capability to provide its proposed services. Therefore, Staff recommends that the Applicant's application for a CC&N to provide intrastate telecommunications services, as listed in Section 2.2 of this Report, be granted subject to the following recommendations:

1. That, unless it provides services solely through the use of its own facilities, the Applicants procure an Interconnection Agreement, within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission, before being allowed to offer local exchange service;

2. That the Applicants file with the Commission, within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission, its plan to have its customers' telephone numbers included in the incumbent's Directories and Directory Assistance databases;

3. That the Applicants pursue permanent number portability arrangements with other LECs pursuant to Commission rules, federal laws and federal rules;

4. That the Applicants agree to abide by and participate in the AUSF mechanism instituted in Decision No. 59623, dated April 24, 1996 (Docket No. RT-00000E-95-0498);

5. That the Applicants abides by the quality of service standards that were approved by the Commission for Qwest in Docket No. T-01051B-93-0183;

6. That in areas where the Applicants are the sole provider of local exchange service facilities, the Applicants will provide customers with access to alternative providers of service pursuant to the provisions of Commission rules, federal laws and federal rules;

7. That the Applicants be required to certify, through the 911 service provider in the area in which it intends to provide service, that all issues associated with the provision of 911 service have been resolved with the emergency service providers, within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission;

8. That the Applicants be required to abide by all the Commission decisions and policies regarding CLASS services;

9. That the Applicants be required to provide 2-PIC equal access;

10. That the Applicants be required to certify that all notification requirements have been completed prior to a final determination in this proceeding;

11. That the Applicants be required to notify the Commission immediately upon changes to the Applicant's address or telephone number;

12. That the Applicants comply with all Commission rules, orders, and other requirements relevant to the provision of intrastate telecommunications service;

13. That the Applicants maintain its accounts and records as required by the Commission;

14. That the Applicants file with the Commission all financial and other reports that the Commission may require, and in a form and at such times as the Commission may designate;

15. That the Applicants maintain on file with the Commission all current tariffs and rates, and any service standards that the Commission may require;

16. That the Applicants cooperate with Commission investigations of customer complaints;

17. That the Applicants participates in and contributes to a universal service fund, as required by the Commission; and

18. Staff obtained information from the Applicants regarding its fair value rate base. Xspedius Switched reported its fair value rate base to be approximately $2.3 million. Xspedius Pima reported its fair value rate base to be approximately $13.6 million. However, the rate to be ultimately charged by the Applicants will be heavily influenced by the market. Because of the nature of the competitive market and other factors, a fair value analysis is not necessarily representative of the Applicants' operations. Therefore, while Staff considered the fair value rate base information submitted by the Applicants, Staff recommends that it not be accorded substantial weight in its analysis of this matter.

    The Applicants lack the market power to adversely affect the interexchange telecommunications market by either restricting output or raising prices. Also, Staff has recommended that the Applicant's services be classified as competitive and thus subject to the flexible pricing authority allowed by the Commission's Competitive Telecommunications Services rules. These two factors, lack of market power and the competitive marketplace for the services the Applicants

proposed to offer, support the conclusion that a fair value analysis is not necessarily representative of the company's operations, and that the rates charged by the Applicants will be reasonable.

Staff further recommends that the Applicants' applications for a CC&N to provide intrastate telecommunications services should be granted subject to the following conditions:

1. The Applicants should be ordered to file conforming tariffs within 365 days from the date of an Order in this matter or 30 days prior to providing service, whichever comes first, and in accordance with the Decision;

2. In order to protect the Applicants' customers,

   a. each Applicant should be ordered to procure a performance bond equal to $235,000;

   b. the minimum bond amount of $235,000 per Applicant should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The bond amount should be increased in increments of $117,500. This increase should occur when the total amount of the advances, deposits, and prepayments is within $23,500 of the bond amount;

   c. if the Applicant desires to discontinue service, it should file an application with the Commission pursuant to AAC R14-2-1107;

   d. the Applicant should be required to notify each of its local exchange customers and the Commission 60 days prior to filing an application to discontinue service; and any failure to do so should result in forfeiture of the Applicant's performance bond;

   e. proof of the performance bond should be docketed within 365 days of the effective date of an Order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission; and

   f. if at some time in the future the Applicant does not collect from its customers an advance, deposit, and/or prepayment, Staff recommends that the Applicant be allowed to file a request for cancellation of its established performance bond regarding its resold interexchange service. Such request should be filed with the Commission for Staff review. Upon receipt of such filing and after Staff review, Staff will forward its recommendation to the Commission.

3. If any of the above timeframes are not met the Applicants, the Applicants' CC&N shall be null and void without further Order of the Commission and no time extensions for compliance shall be granted.

6.2 RECOMMENDATION OF THE APPLICANTS' PETITION TO HAVE ITS PROPOSED SERVICES CLASSIFIED AS COMPETITIVE

Staff believes that the Applicants' proposed services should be classified as competitive. There are alternatives to the Applicants' services. The Applicants will have to convince customers to purchase its services, and the Applicants have no ability to adversely affect the local exchange or interexchange service markets. Therefore, the Applicants currently have no market power in the local exchange or interexchange service markets where alternative providers of telecommunications services exist. Staff therefore recommends that the Applicants' proposed services be classified as competitive.

Staff further recommends that the Applicants be subject to the Commission's rules governing interconnection and unbundling and the 1996 Telecommunications Act and the rules promulgated thereunder. In the event that the Applicants provide essential services or facilities that potential competitors need in order to provide their services, the Applicants should be required to offer those facilities or services to these providers on non-discriminatory terms and conditions pursuant to federal laws, federal rules, and state rules.

6.3 RECOMMENDATIONS OF THE PETITIONERS' TRANSFER OF ASSETS

The following Staff recommendations will help ensure the assets of e.Spire Operating Entities are transferred in an ordering manner to the Xspedius Operating Entities:

1. That a hearing be scheduled to approve the transfer of assets as soon as possible due the emergency nature of the application.

2. That e.Spire Operating Entities' ensure the affected customers receive proper discontinue service notification in full compliance with AAC R14-2-1107, and upon such notice the customers may elect within 90 days (of the Order) to continue or discontinue service in their discretion, without prejudice or regard to contractual obligation

SERVICE LIST FOR: ACSI LOCAL SWITCHED SERVICES, INC. DBA E.SPIRE AND AMERICAN COMMUNICATION SERVCIES OF PIMA COUNTY, INC. DBA E.SPIRE, XSPEDIUS MANAGEMENT CO. SWITCHED SERVICES LLC, AND XSPEDIUS MANAGEMENT CO. OF PIMA COUNTY, L.L.C.
DOCKET NOS. T-04112A-02-0450, T-04113A-02-0450 T-03597A-02-0450, T-03411A-02-0450, T-04112A-02-0451 AND T-04112A-02-0452

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