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MEMORANDUM

TO: Docket Control
FROM: Steven M. Olea
Director
Utilities Division

DATE: December 2, 2014

RE: IN THE MATTER OF THE APPLICATION OF BCN TELECOM, INC. FOR APPROVAL OF A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE RESOLD LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES. (DOCKET NO. T-04057A-13-0270)

Arizona Corporation Commission
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Attached is the Staff Report for the above referenced application, as amended. The Applicant is seeking Commission approval to provide the following services:

- Resold Local Exchange Services
- Facilities-Based Local Exchange Services

Staff is recommending approval of the application with conditions.

SMO:LLM:red\BES

Originator: Lori Morrison

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DOCKET NO. T-04057A-13-0270

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STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

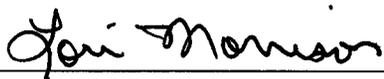
BCN TELECOM, INC.
DOCKET NO. T-04057A-13-0270

IN THE MATTER OF THE APPLICATION OF BCN TELECOM, INC. FOR APPROVAL OF
A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE RESOLD LOCAL
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DECEMBER 2, 2014

STAFF ACKNOWLEDGMENT

The Staff Report for BCN Telecom, Inc., Docket No. T-04057A-13-0270, was the responsibility of the Staff member listed below. Lori Morrison was responsible for the review and analysis of the application for a Certificate of Convenience and Necessity to provide resold and facilities-based local exchange telecommunications services and petition for a determination that its proposed services should be classified as competitive.

A handwritten signature in cursive script that reads "Lori Morrison". The signature is written in black ink and is positioned above a horizontal line.

Lori Morrison
Utilities Consultant

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1. INTRODUCTION AND BACKGROUND

On August 7, 2013, BCN Telecom, Inc. (“BCN” or “Applicant” or “Company”) filed an application for a Certificate of Convenience and Necessity (“CC&N”) to provide resold local exchange telecommunications services on a statewide basis in Arizona. The Applicant petitioned the Arizona Corporation Commission (“ACC” or “Commission”) for a determination that its proposed services should be classified as competitive.

On April 25, 2014, the Applicant filed an Amended Application to include facilities-based local exchange telecommunications services to the list of services for which it is seeking a CC&N. On October 24, 2014, the Applicant filed an Amended Application Attachment C-2 to remove an inadvertent inclusion of Mr. John Kean, Jr. within the Attachment.

BCN currently holds a CC&N to provide resold long distance telecommunications services granted on June 5, 2002, in Decision No. 64894.

Staff’s review of this application addresses the overall fitness of the Applicant to receive a CC&N. Staff’s analysis also considers whether the Applicant’s services should be classified as competitive, if the Applicant’s initial rates are just and reasonable and if approval of the Applicant’s CC&N should be conditioned.

2. REQUESTED SERVICES

BCN’s CC&N application requested statewide authority to provide resold and facilities-based local exchange telecommunications services. Staff reviewed the Applicant’s amended tariff, filed September 16, 2014, that listed the proposed rates, charges, prices, terms and conditions for service to business customers.

3. TECHNICAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

BCN is a privately held, foreign corporation organized under the laws of New Jersey, headquartered in Bedminster, NJ. The Applicant requests the authority to provide resold and facilities-based basic local exchange services to business customers in Arizona. BCN states that it will not have any employees located in Arizona.

BCN currently has authority in forty-two jurisdictions¹ to provide local exchange and interexchange telecommunications services and authority to provide interexchange telecommunications services in seven jurisdictions,² excluding Arizona. BNC has applications

¹ Response to Staff Data Request STF 1.8. Alabama, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kentucky, Maine, Maryland, Massachusetts, Michigan, Minnesota, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin and Wyoming.

² Response to Staff Data Request STF 1.8. Arkansas, Hawaii, Kansas, Louisiana, Mississippi, Missouri, and Oklahoma

pending in five other jurisdictions³ for authority to provide local exchange services. The combined telecommunications experience of BCN's top six executives is over 116 years.

Based on the above information, Staff believes BCN possesses the technical capabilities to provide the services it is requesting the authority to provide in Arizona.

4. FINANCIAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

The Applicant provided unaudited financial statements for the twelve months ending December 31, 2012, and twelve months ending December 31, 2013. The unaudited financial statements as of December 31, 2012, list total assets of \$10,126,391, total equity of \$913,238, and a net income of negative \$585,245. The unaudited financial statements ending December 31, 2013, list total assets of \$9,575,542, total equity of \$578,704, and a net income of negative \$302,909. The Applicant did not provide notes related to the financial statements.

5. ESTABLISHING RATES AND CHARGES

The Applicant would initially provide service in areas where an incumbent local exchange carrier ("ILEC"), along with various competitive local exchange carriers ("CLECs"), are providing telephone service. Therefore, the Applicant would have to compete with those providers in order to obtain subscribers to its services. The Applicant 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 Applicant would generally not be able to exert market power. Thus, the competitive process should result in rates that are just and reasonable.

Both an actual rate and a maximum rate may be listed for each competitive service offered. The rate charged for a service may not be less than the Applicant's total service long-run incremental cost of providing the service pursuant to A.A.C. R14-2-1109.

The rates proposed by this filing are for competitive services. In general, rates for competitive services are not set according to rate of return regulation. In response to section B-4 of its amended application, the Applicant provided an estimated net book value or fair value rate base at the end of its first 12 months of operation of zero (\$0).

On September 16, 2014, BCN submitted amended Arizona Tariff Nos. 2 and 3 to support its amended application. Staff has reviewed these rates and believes they are comparable to the rates charged by CLECs, ILECs and major long distance carriers operating in the State of Arizona. The Applicant's rates and charges are also comparable to the rates and charges the Applicant charges in other state jurisdictions. The rate to be ultimately charged by the Applicant will be heavily influenced by the market. Therefore, while Staff considered the fair value rate base information submitted by the Applicant, the fair value rate base information provided was not given substantial weight in this analysis.

³ Response to Staff Data Request STF 1.8. Arkansas, Kansas, Louisiana, Mississippi and Missouri.

6. LOCAL EXCHANGE CARRIER SPECIFIC ISSUES

Issues related to the provision of Local Exchange service are discussed below.

6.1 Number Portability

The Commission has adopted rules to address number portability in a competitive telecommunications services market. Local exchange competition may not be vigorous if customers, especially business customers, must change their telephone numbers to take advantage of a CLEC's service offerings. Consistent with federal laws, federal rules and A.A.C. R14-2-1308(A), the Applicant shall make number portability available to facilitate the ability of a customer to switch between authorized local carriers within a given wire center without changing their telephone number and without impairment to quality, functionality, reliability or convenience of use.

6.2 Provision of Basic Telephone Service And Universal Service

The Commission has adopted rules to address universal telephone service in Arizona. A.A.C. R14-2-1204(A) indicates that all telecommunications service providers that interconnect into the public switched network shall provide funding for the Arizona Universal Service Fund ("AUSF"). The Applicant will make the necessary monthly payments required by A.A.C. R14-2-1204(B).

6.3 Quality of Service

In the competitive market that the Applicant wishes to enter, the Applicant 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 the Applicant should be ordered to abide by the same quality of service standards that were approved by the Commission for Qwest Corporation dba CenturyLink QC ("Qwest") in Docket No. T-01051B-13-0199 (Decision No. 74208).

6.4 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. There may be areas where the Applicant installs the only local exchange service facilities. In the interest of providing competitive alternatives to the Applicant's local exchange service customers, Staff recommends that the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve such areas. This way, an alternative local exchange service provider may serve a customer if the customer so desires. 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.

6.5 911 Service

The Commission has adopted rules to address 911 and E911 services in a competitive telecommunications services market. The Applicant has certified that, in accordance with A.A.C. R14-2-1201(6)(d) and Federal Communications Commission 47 CFR Sections 64.3001 and 64.3002, it will provide all customers with 911 and E911 service, where available, or will coordinate with ILECs and emergency service providers to provide 911 and E911 service.

6.6 Custom Local Area Signaling Services

Consistent with past Commission decisions, the Applicant may offer Caller ID provided that per call and line blocking, with the capability to toggle between blocking and unblocking the transmission of the telephone number, are provided as options to which customers could subscribe with no charge. Also, Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated, indicating that the number has been blocked, must be offered.

7. REVIEW OF COMPLAINT INFORMATION

In the Amended Application, the Applicant states that it has neither had an application for service denied, nor had its authority to provide service revoked in any jurisdiction. Staff did not find any instances of denied applications or revocation of authority to provide service.

In response to whether the Applicant or any of its officers, directors or partners have been or are currently involved in any formal or informal complaint proceedings pending before any state or federal regulatory commission, administrative agency or law enforcement agency, the Applicant provided the following in Attachment C-1 of its amended application addressing jurisdictional complaints and noncompliance:

Federal Communications Commission

Applicant was involved with an informal complaint filed with the Federal Communications Commission ("FCC") in 2011 in IC No. 09-S0295710. The FCC received a complaint on April 9, 2009, alleging that a Complainant's telecommunications service provider had been changed to WorldCom without the Complainant's authorization. The FCC notified MCI of the complaint because WorldCom no longer existed and MCI responded May 28, 2009. Based on MCI's response, the FCC notified Verizon of the complaint and Verizon responded September 17, 2009. Based on Verizon's response, the FCC purportedly notified BCN of the complaint. Due to lack of notice, BCN failed to respond. As a result, the FCC granted the informal complaint.

A search of the FCC website found, other than the complaint discussed above, there have been no other complaints against the Applicant.

Maryland

On October 8, 2012, the Maryland Public Service Commission ("MD PSC") issued an Order to Show Cause in Case No. 9302, *In the Matter of the Investigation by the Commission of the Telecommunications companies' Failure to Comply with the Commission's May 11, 2012 Notice*

of Required Tariff Filings, which included the Applicant. Applicant worked diligently with Staff in order to comply with the MD PSC Order. In the time period required for the calculations, Applicant had no terminating minutes of use. In fact, the terminating revenues for the period at issue would be zero (\$0.00). Notwithstanding, in an effort to comply with the MD PSC Order, Applicant submitted Tariff revisions sent via FedEx August 10, 2012; the MDPSC stamped "Filed" the pages submitted in this matter August 13, 2012.

Staff contacted the MD PSC Staff who advised that BCN's tariff revisions were accepted by the MD PSC on October 17, 2012, and BCN is compliant with MD PSC filing requirements/Order to Show Cause in the referenced matter. There were no penalties assessed on BCN.

South Carolina

Petition of the Office of Regulatory Staff for Commission to Order a Rule to Show Cause as to Why the Certificates of Public Convenience and Necessity for Certain Providers of Telecommunications Services Should Not Be Revoked, Docket No. 2011-466-C, for failure to file certain State USF reports. Applicant submitted the required reports and was dismissed from Show Cause proceeding.

Staff contacted the South Carolina Public Service Commission ("SC PSC") Staff who advised that, in a Rule to Show Cause proceeding, if a company does not resolve its non-compliance, the resultant penalty is the revocation of the company's Certificate of Public Convenience and Necessity. In the case of BCN Telecom, BCN failed to timely file a gross receipts report but resolved the matter by filing the required report.

West Virginia

West Virginia Public Service Commission ("WV PSC") entered an Investigation of Failure to File Annual Reports, Case No. 04-1400-T-SC. On August 27, 2004, the WV PSC opened a docket. Applicant failed to timely file the 2003 Annual Reports. The case was referred to the Division of Administrative Law Judges for further proceedings. On January 26, 2005, Applicant filed its 2003 Annual Report explaining that it was the Company's understanding that since no services were provided in West Virginia, the Annual Report did not need to be filed.

Staff contacted the WV PSC Staff who provided a copy of the WV PSC's Order, issued February 23, 2005, which concluded that, since BCN had filed the 2003 Annual Report which was the subject of the proceeding, the recommended fine of \$500 for failure to file the report be waived, and the proceeding be removed from the WV PSC's active docket of cases.

Other than those matters discussed above, Staff has found no other instances of any formal or informal complaint proceedings pending before any state or federal regulatory commission, administrative agency or law enforcement agency involving the Applicant or any of its officers, directors or managers.

In response to whether any of the Applicant's officers, directors or partners have been or are currently involved in any civil or criminal investigations, or had judgments levied by any

administrative or regulatory agency, or been convicted of any criminal acts in the past ten (10) years, the Applicant provided the following in Attachment C-2 of its Amended Application addressing civil or criminal investigations, judgments or convictions:

Joseph Nacchio resigned as a member⁴ of the Board of Directors of BCN Telecom, Inc. on August 1, 2005,⁵ due to being federally indicted on insider-trading charges.

Staff's review of Mr. Nacchio's federal indictment⁶ on insider-trading charges led it to the conclusion that the charges are not related to BCN. Instead, the indictment is related to Mr. Nacchio's former employer and his tenure⁷ as CEO of Qwest Communications International, Inc. ("Qwest"). Mr. Nacchio resigned from BCN's Board of Directors in 2005 and the indictment against him was not related to his involvement with BCN.

The Applicant has currently been granted authority in forty-two jurisdictions to provide local exchange and interexchange telecommunications services and authority to provide interexchange telecommunications services in seven jurisdictions, excluding Arizona, as discussed above. Staff contacted ten⁸ other jurisdictions to verify certification to provide service and to inquire about complaints. The ten jurisdictions advised that the Applicant was indeed authorized to provide service in their jurisdiction and that no complaints had been received about the Applicant.

The Corporations Division has indicated that BCN is in good standing. The Consumer Services Section reports no complaints have been filed in Arizona from January 1, 2010 to August 14, 2013.

8. COMPETITIVE SERVICES ANALYSIS

The Applicant has petitioned the Commission for a determination that the services it is seeking to provide should be classified as competitive.

8.1 *Competitive Services Analysis for Local Exchange Services*

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

The statewide local exchange market that the Applicant seeks to enter is one in which a number of CLECs have been authorized to provide local exchange service in areas previously served only by ILECs. At locations where ILECs provide local exchange service, the Applicant will be entering the market as an alternative provider of local exchange service and, as such, will have to compete with those existing

⁴ Mr. Nacchio was a member of BCN Telecom, Inc.'s Board for Directors from December 2003 to August 2005, per email from PCrocker, Attorney for BCN Telecom, Inc., September 10, 2014.

⁵ Clarification from summer of 2005 provided via email from PCrocker, Attorney for BCN Telecom, Inc., September 15, 2014.

⁶ *United States v. Nacchio*, Criminal Action No. 05-CR-00545-MSK Indictment, U.S. Dist. Ct. CO. (2005).

⁷ December 1996 to June 2002. From <http://www.huffingtonpost.com/huff-wires/20100422/us-qwest-timeline/>

⁸ California, Colorado, Florida, Iowa, Nevada, New Mexico, New York, Pennsylvania, Washington and Wisconsin.

companies in order to obtain customers. In areas where ILECs do not serve customers, the Applicant may have to convince developers to allow it to provide service to their developments. The areas served by CenturyLink that the Applicant seeks to enter are served by wireless carriers and Voice over the Internet Protocol ("VoIP") service providers. This may also be the case in areas served by independent ILECs.

8.1.2 The number of alternative providers of the service.

CenturyLink and various independent ILECs provide local exchange service in the State. CLECs and local exchange resellers are also providing local exchange service. The areas served by CenturyLink that the Applicant seeks to enter are served by wireless carriers and VoIP service providers. This may also be the case in portions of the independent ILECs' service territories.

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

CenturyLink and CLECs are the primary providers of local exchange service in CenturyLink's Service territories. Independent ILECs are the primary providers of local exchange service in their service territories.

8.1.4 The names and addresses of any alternative providers of the service that are also affiliates of the Applicant, as defined in A.A.C. R14-2-801.

BCN does not have any affiliates that are alternative providers of local exchange service in Arizona.

8.1.5 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 Applicant has requested the authority to provide in their respective service territories. Similarly, many of the CLECs, local exchange service resellers, wireless carriers and VoIP service providers also offer substantially the same services.

8.1.6 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. Competition exists in most urban markets, but to a lesser degree in rural areas of the state.

- b. One in which new entrants will be dependent upon ILECs and other CLECs:
 - 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 existing ILECs and CLECs have had an existing relationship with their customers that the Applicant will have to overcome if it wants to compete in the market and one in which the Applicant will not have a history in the Arizona local exchange service market.
- d. One in which the Applicant will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

9. RECOMMENDATIONS

The following sections contain the Staff recommendations on the application for a CC&N and the Applicant's petition for a Commission determination that its proposed services should be classified as competitive.

9.1 Recommendations on the Application for a CC&N

Staff recommends that Applicant's application for a CC&N to provide intrastate telecommunications services, as listed in this Report, be granted. In addition, Staff further recommends:

- 1. That the Applicant comply with all Commission Rules, Orders and other requirements relevant to the provision of intrastate telecommunications services;
- 2. That the Applicant abide by the quality of service standards that were approved by the Commission for Qwest in Docket No. T-01051B-13-0199 (Decision No. 74208);
- 3. That the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve areas where the Applicant is the only provider of local exchange service facilities;
- 4. That the Applicant be required to notify the Commission immediately upon changes to the Applicant's name, address or telephone number;
- 5. That the Applicant cooperate with Commission investigations including, but not limited to, customer complaints;
- 6. The rates proposed by this filing are for competitive services. In general, rates for competitive services are not set according to rate of return regulation. The Applicant

estimated a net book value or fair value rate base at the end of its first 12 months of operation to be zero (\$0). Staff has reviewed the rates to be charged by the Applicant and believes they are just and reasonable as they are comparable to other providers offering service in Arizona and comparable to the rates the Applicant charges in other jurisdictions. The rate to be ultimately charged by the Applicant will be heavily influenced by the market. Therefore, while Staff considered the fair value rate base information submitted by the Applicant, the fair value information provided was not given substantial weight in this analysis;

7. That the Applicant offer Caller ID with the capability to toggle between blocking and unblocking the transmission of the telephone number at no charge;
8. That the Applicant offer Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated; and
9. That the Commission authorize the Applicant to discount its rates and service charges to the marginal cost of providing the services.

Staff further recommends that the Applicant be ordered to comply with the following. If it does not do so, the Applicant's CC&N shall be null and void, after due process:

1. The Applicant shall docket a conforming tariff for each service within its CC&N within 365 days from the date of an Order in this matter or 30 days prior to providing service, whichever comes first;
2. The Applicant shall notify the Commission through a compliance filing within 30 days of the commencement of service to end-user customers; and
3. The Applicant shall abide by the Commission adopted rules that address Universal Service in Arizona. A.A.C. R14-2-1204(A) indicates that all telecommunications service providers that interconnect into the public switched network shall provide funding for the Arizona Universal Fund. The Applicant will make the necessary monthly payments required by A.A.C. R14-2-1204 (B).

9.2 Recommendation on the Applicant's Petition to Have Its Proposed Services Classified as Competitive

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