

Decision 01-03-079 March 27, 2001

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

In re Request of WORLDCOM, INC. and  
INTERMEDIA COMMUNICATIONS INC., For  
Approval to Transfer Control of Intermedia  
Communications Inc. and its Wholly-owned  
Subsidiary to WorldCom, Inc.

Application 00-11-048  
(Filed November 11, 2000)

**O P I N I O N**

**1. Summary**

This decision grants the application of WorldCom, Inc. (WorldCom) and Intermedia Communications, Inc. (Intermedia) (collectively, Applicants) to merge their operations, subject to certain conditions.

**2. The Application**

WorldCom and Intermedia filed this application on November 11, 2000. They seek Commission approval to transfer control to WorldCom of Intermedia and its wholly-owned subsidiary, Access Network Services Inc. (ANSI), and implement an Agreement and Plan of Merger (Merger Agreement) executed on September 1, 2000. WorldCom will acquire control of Intermedia and ANSI, but the transaction will not involve the transfer of certificates, assets or customers to

a new entity. Intermedia and ANSI will continue to hold these certificates<sup>1</sup> and to operate in California pursuant to their existing rates, terms and conditions.

The Merger Agreement provides that Wildcat Acquisition Corp. (Wildcat) a wholly-owned, Delaware subsidiary of WorldCom formed to effect the transaction,<sup>2</sup> will merge with and into Intermedia, and Intermedia will be the surviving corporation. Intermedia, as the surviving company following the merger, will become a subsidiary of WorldCom upon completion of the transaction. ANSI will retain the same corporate relationship with Intermedia as it has currently, and will therefore become an indirect subsidiary of WorldCom.

Applicants assert the merger will have limited impact on the California telecommunications market because Intermedia does little business in the state. According to the application, Intermedia and its subsidiaries have fewer than 350 business customers in California and only approximately 175 residential long distance customers, all of whom are affiliated with the companies' business customers. Neither Intermedia nor ANSI currently provides local exchange service in California, although they are authorized to do so. As of June 30, 2000, Intermedia's 2000 revenues from California intrastate long distance services were \$216,000, or less than 0.1 percent of the company's total revenues.

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<sup>1</sup> Intermedia was granted authority to provide competitive local exchange carrier services on February 3, 2000 in Decision (D.) 00-02-013 (Corp. ID No. U-6302-C) and to provide interexchange services on December 20, 1996 in D.96-12-047 (Corp. ID No. U-5713-C). ANSI was granted authority to provide interexchange services on May 4, 1990 in D.90-05-014, Application (A.) 89-10-040.

<sup>2</sup> Wildcat is not qualified to do business in California, but the entity will cease to exist once the transaction occurs.

### 3. U.S. Justice Department Lawsuit

An issue not raised directly in the application, but of concern to this Commission, has to do with the extent to which WorldCom and Intermedia are both important providers in the Internet backbone market. Indeed, the U.S. Justice Department (Justice Department) recently filed – and settled – an antitrust lawsuit (Lawsuit) challenging the merger on the ground that it would result in undue concentration in that market.<sup>3</sup> Therefore, on December 28, 2000, the assigned Administrative Law Judge (ALJ) issued a ruling to the parties seeking input on the impact of the Justice Department’s Lawsuit on this proceeding.<sup>4</sup> The ruling asserted that California has jurisdiction to consider the merger’s impact on the Internet backbone market to the extent it effects California consumers.

While Applicants took issue with the ALJ’s claim of Commission jurisdiction, they explained that the Justice Department’s settlement (Settlement Agreement) of the Lawsuit eliminated any concerns about the merger’s effect on the Internet backbone market. As part of the Settlement Agreement, WorldCom agreed that it would neither obtain nor have control over or interest in Intermedia’s facilities used to provide Internet backbone services. Rather, WorldCom will hold those facilities separately following the closing of the WorldCom-Intermedia transaction and divest them to a third party or parties within 180 days of the closing. Thus, Applicants claim, the current merger will not consolidate or merge any of the Internet backbone services offered by

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<sup>3</sup> *U.S. v. WorldCom, Inc. and Intermedia Communications, Inc.*, Civil Action No. 2789, Case No. 1:00CV02789(RWR) (D.D.C., filed Nov. 17, 2000).

<sup>4</sup> *Administrative Law Judge’s Ruling Regarding Effect of U.S. v. WorldCom, Inc. and Intermedia Communications, Inc.*, mailed December 28, 2000.

Intermedia with those offered by WorldCom's existing subsidiaries.<sup>5</sup> We agree that the Settlement Agreement alleviates our concerns about the merger's effects on the Internet backbone market.

We grant the application contingent on and subject to all conditions in the Settlement Agreement. Moreover, the application states that "WorldCom will seek Commission authorization at such time as it enters into an agreement to sell all or a portion of the jurisdictional assets owned and operated by Intermedia."<sup>6</sup> We will hold WorldCom to this commitment as well.

#### **4. Applicants' Request for Waiver of Pub. Util. Code §§ 854(b) and (c)**

Concurrent with the application, Applicants sought a waiver of Pub. Util. Code §§ 854(b) and (c) pursuant to § 853(b). Sections 854(b) and (c) require that the Commission review certain large mergers to determine their competitive, consumer and other impacts. On its face, § 854(b) applies where any party to a proposed merger or acquisition has gross annual California revenues exceeding \$500,000,000. We know from the application that Intermedia's California revenues do not even approach this magnitude, so we assume it is WorldCom's revenues that bring the merger within the purview of the statute.

Applicants assert that this Commission has devised a three-part test for exempting large mergers from §§ 854(b) and (c).<sup>7</sup> In a recent decision on

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<sup>5</sup> Applicants furnished copies of the Justice Department's antitrust complaint and the Settlement Agreement. These documents appear as Appendices A and B to this decision, respectively.

<sup>6</sup> Application at 7.

<sup>7</sup> According to Applicants, waiver is justified when (1 the transaction does not combine traditionally regulated telephone companies; 2) the applicants are not rate regulated; and 3) applicants have grown under competitive forces without a captive ratepayer

*Footnote continued on next page*

WorldCom's now-defunct merger with Sprint Corporation (Sprint), the Commission affirmed an earlier ruling of the assigned ALJ declining to waive §§ 854(b) and (c)'s application to that merger.<sup>8</sup> The ruling had disagreed with WorldCom's contention that the Commission has established a hard and fast rule applicable to such waivers.

Here, therefore, Applicants allege that waiver is justified despite the determination in the WorldCom-Sprint merger case. They reason that the Commission refused to waive §§ 854(b) and (c) in that case on the ground that the size of the proposed MCI WorldCom-Sprint merger, and its potential effect on competition in the long distance market (particularly on residential customers), warranted full review under §§ 854(b) and (c). Moreover, the Commission declined the waiver request because both WorldCom and Sprint had significant California market share. According to Applicants, the WorldCom-Intermedia merger, in contrast, "is much smaller by every measure -- dollar value, customers affected, effect on the California market -- than . . . those transactions exempted in prior Commission decisions and cited by the ALJ."

We do not believe that mergers involving at least one party with \$500,000,000 in California revenues automatically should be excused from the requirements of §§ 854(b) and (c) simply because the acquired party does little business in California. For example, if an acquired party, while small, were the acquirer's only competitor in California, then it might make sense to apply

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base *Id.* at 20, citing D.00-05-023, D.99-03-019, D.98-08-068, D.98-05-022 and D.97-05-092, *aff'd*, D.97-07-060.

<sup>8</sup> D.01-02-040 (February 9, 2001).

§§ 854(b) and (c) to that transaction. By the same token, the waiver statute appears to give us discretion to decide on a case-by-case basis whether waiver is appropriate. Section 853(b) provides that,

The commission may from time to time by order . . . exempt any public utility . . . from this article if it finds that the application thereof with respect to the public utility is not necessary in the public interest.

Commission precedent indicates that this provision must be applied selectively as it must be the exception and not the rule. There are several factors justifying waiver in this case. First, the settlement of the Justice Department Lawsuit discussed in Section 3 above illustrates that, at least as to the Internet backbone, the merger will simply preserve the *status quo* until subsequent transactions are concluded. Thus, there will be another opportunity to review the transaction when it is ultimately completed. WorldCom's share of that market will not increase because Intermedia's Internet backbone market assets will be sold off to a third party. Thus, the one significant effect that the merger might have on California consumers has been mitigated by the Justice Department settlement. In a similar vein, the merger will preserve Intermedia as a player - albeit a small one - in the California market, thereby preventing the disruption to California customers and employees that might result from Intermedia's demise.

Second, Intermedia primarily serves business customers, a market where there is a great deal of competition. Thus, WorldCom's acquisition of Intermedia will not have an impact on a market - such as the residential market - in which consumers have few alternatives. Nor will the merger eliminate the sole competitor in the marketplace, or one of the few choices available to customers.

Third, Intermedia's small number of customers, dollar revenues, and number of employees in California persuade us that there would be little benefit to conducting a full Section 854(b) and (c) review in this case. At maximum, the merger preserves a company with approximately \$200,000 in California revenue, a drop in the bucket for the California telecommunications market. It is hard to imagine how WorldCom, a company with California revenues in excess of \$500 million, could possibly harm California consumers or employees in any material way by growing its California business by \$200,000.

The foregoing factors in combination persuade us that waiver is appropriate in this case. This decision is limited to the facts of this case, and is not intended to be precedential.

Just because we waive §§ 854(b) and (c) does not mean that we should not examine the transaction to ensure that it promotes the interests of California ratepayers. In the next section, we do just that, and conclude that the merger should be allowed.

## **5. Public Interest**

Applicants claim the merger is in the public interest because it will result in an infusion of capital for Intermedia, which has recently suffered financial problems due to a general downturn in the competitive local exchange carrier (CLEC) market. (While Intermedia is certificated as a CLEC in California, it does not currently serve local exchange customers in the state. It does so in other states, however.) According to the application,

CLECs in general, and Intermedia in particular, do not currently have access to public and private equity and debt markets at favorable rates, terms and conditions to enable them to raise the capital necessary to develop their networks and to expand their businesses . . . . Intermedia's stock has fallen from its high of \$77 in

March of this year to the mid-20s in July, and to less than \$15 in August, shortly before this transaction was announced.<sup>9</sup>

Thus, Applicants' public interest argument is based on Intermedia's need for WorldCom financial support.

The public interest test is set forth in § 854(a), and provides that,

No person or corporation, whether or not organized under the laws of this state, shall merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state without first securing authorization to do so from the Commission.

The Commission has interpreted § 854(a) to require a determination of whether the transaction serves the public interest.

Applicants' public interest argument relies principally on the theory that it is in the interest of California consumers not to have Intermedia fail – *i.e.*, that the merger will *not be adverse to the public interest*. Applicants cite a line of cases they allege establish that “The primary question to be determined in a transfer of control proceeding under § 854(a) is whether the proposed transfer would be adverse to the public interest.”<sup>10</sup>

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<sup>9</sup> Application at 11.

<sup>10</sup> Application at 9-10, citing *In the Matter of the Joint Application of AT&T Corp., Meteor Acquisition Inc., and MediaOne Group, Inc.*, D.00-05-023, 2000 Cal. PUC LEXIS 355, May 4, 2000, at \*24-\*25; *In the Matter of the Joint Application of AT&T Corp., Italy Merger Corp. and Tele-Communications, Inc.*, D.99-03-019, 1999 Cal. PUC LEXIS 382, March 4, 1999, at \*22; *In re Application of WorldCom, Inc. and MCI Communications Corporation*, D.98-08-068, 1998 Cal. PUC LEXIS 912, August 31, 1998, at \*34; *In re Joint Application of AT&T Corp. ("AT&T"), Teleport Communications Group Inc. ("TCG") and TA Merger Corp.*, D.98-05-022, 1998 Cal. PUC LEXIS 533, May 7, 1998, at \*12; all citing *M. Lee (Radio Paging)*, 65 CPUC 635 (1966).

However, Applicants recognize that some Commissioners recently have stated that mergers should not only avoid public harm, but should also produce *positive and substantive benefits for California ratepayers*.<sup>11</sup> While Applicants argue that those cases are not relevant here, they also attempt to show a positive ratepayer benefit. However, this “benefit” – the bolstering of Intermedia in uncertain economic times – is identical to the factor Applicants cite to establish that the proposed transfer is not adverse to the public interest.

In this case, we believe Intermedia’s business dealings in California are so insignificant as to render sufficient Applicants’ public interest showing. However, we caution Applicants and others that we may not always accept a showing based on absence of public harm – rather than on presence of public benefits – in the future. We are prepared to scrutinize mergers carefully to ensure that mergers provide such benefits.

By the same token, there is one positive benefit to California ratepayers that Applicants did not cite – and we believe it bolsters the public interest showing here. The CLEC market – once robust – is faltering. We believe that competition in telecommunications is a good thing, and that, where it has flourished, competition has exerted downward pressure on consumer prices. While allowing WorldCom to acquire control of Intermedia does not preserve a competitor in the literal sense, we believe an acquisition is preferable to having Intermedia simply disappear from the landscape.

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<sup>11</sup> Application at 10, citing D.00-05-027, at (Commrs Lynch and Wood, concurring) (decision available at [http://www.cpuc.ca.gov/PUBLISHED/FINAL\\_DECISION/438.htm](http://www.cpuc.ca.gov/PUBLISHED/FINAL_DECISION/438.htm); D.00-05-047, 2000 Cal. PUC LEXIS 314, May 18, 2000, at \*51-\*53 (Commr Lynch dissenting).

Thus, we find that the transaction is in the public interest, and produces positive benefits for ratepayers.

## **6. Conclusion**

We find that the merger serves the public interest and should be granted.

## **7. Waiver of Comment Period**

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Pub. Util. Code § 311(g)(2), the otherwise applicable 30-day period for public review and comment is being waived.

## **Findings of Fact**

1. Notice of this application appeared in the Commission's Daily Calendar of November 21, 2000.
2. Intermedia was granted authority to provide competitive local exchange carrier services on February 3, 2000 in D.00-02-013 (Corp. ID No. U-6302-C) and to provide interexchange services on December 20, 1996 in D.96-12-047 (Corp. ID No. U-5713-C). ANSI was granted authority to provide interexchange services on May 4, 1990 in D.90-05-014, A.89-10-040.
3. There will be no change in services or rates provided by WorldCom, Intermedia or ANSI as a result of the transfer of control. This decision authorizes no change in the services or rates any applicant now offers in California.
4. The transaction will help stabilize the finances of Intermedia.
5. The transaction will have positive benefits for California ratepayers.
6. The Settlement Agreement resolving the Justice Department's Lawsuit against Applicants reasonably protects the Internet backbone market from undue concentration.

**Conclusions of Law**

1. The proposed merger is in the public interest.
2. Waiver of §§ 854(b) and (c) is warranted. This decision is based on the unique facts of this case and has no precedential value.
3. WorldCom should seek Commission authorization at such time as it enters into an agreement to sell all or a portion of the jurisdictional assets owned and operated by Intermedia.
4. All terms of the Settlement Agreement resolving the Justice Department's Lawsuit against Applicants should be incorporated herein and made conditions on our granting of this application.
5. This proceeding is designated a ratesetting proceeding; no protests have been received; no hearing is necessary.
6. The application should be approved.

**O R D E R**

**IT IS ORDERED** that:

1. WorldCom, Inc. (WorldCom) and Intermedia Communications Inc. (Intermedia) (collectively, Applicants) are authorized pursuant to Section 854 of the Public Utilities Code to enter into the transaction, as more fully described in the application and its exhibits, by which WorldCom will acquire control of Intermedia.
2. Applicants shall notify the Director of the Commission's Telecommunications Division in writing of the transfer of authority, as authorized herein, within 10 days of the date of this order. A true copy of the instruments of transfer shall be attached to the notification.

3. Applicants shall file new tariffs incorporating any changes in name, rates, services and management authorized in the transfer transaction.

4. Applicants shall make all books and records available for review and inspection upon Commission staff request.

5. WorldCom shall seek Commission authorization at such time as it enters into an agreement to sell all or a portion of the jurisdictional assets owned and operated by Intermedia.

6. All portions of Hold Separate Stipulation and Order in *United States of America v. WorldCom, Inc., and Intermedia Communications, Inc.*, Civil Action No. 2789, Case No. 1:00CV02789(RWR) (D.D.C., filed Nov. 17, 2000), contained in Appendix A to this decision, are incorporated herein and made conditions to this decision.

7. WorldCom shall hold separately Intermedia's facilities used to provide Internet backbone services following the closing of the WorldCom-Intermedia transaction and divest them to a third party or parties within 180 days of the closing.

8. This proceeding is closed.

This order is effective today.

Dated March 27, 2001, at San Francisco, California

LORETTA M. LYNCH  
President  
HENRY M. DUQUE  
RICHARD A. BILAS  
CARL W. WOOD  
GEOFFREY F. BROWN  
Commissioners