October 5, 2004

VIA HAND DELIVERY

Kristi Izzo, Secretary
New Jersey Board of Public Utilities
Two Gateway Center
Newark, New Jersey 07102

Re: I/M/O The Board's Investigation as to Whether Ratepayers Should Share in the Proceeds Arising From the Sale and Conveyance of Real Property by Verizon New Jersey, Inc.
BPU Docket No. TX04080749

Dear Ms. Izzo:

The New Jersey Division of the Ratepayer Advocate ("Ratepayer Advocate") respectfully submits the following comments for consideration by the New Jersey Board of Public Utilities ("Board") to decide the critical issues presented by the scope of the instant investigation as they relate to the core right of New Jersey ratepayers to share equitably in the proceeds from the sale of utility assets by Verizon New Jersey Inc. ("Verizon NJ"). Enclosed with this original please find ten (10) copies as well as a time/stamp copy for return to the Ratepayer Advocate.[1]

[1] The Ratepayer Advocate ask that the Board clarify that this investigation is intended to cover not only real property sales but all sales of assets. The Board has consistently required sharing of proceeds from sale of assets and not limited such sharing to real property. The Ratepayer Advocate notes the majority of cases do deal with land and improvements to real property.

The amounts in controversy and at stake are material and significant. The sale to Plainfield-Hadley and the sale of the Elizabeth property to Kenneth Esdale alone represent $3.863 million. To date, there are nine (9) other proposed sales of assets that are either approved by the Board or awaiting approval. Exhibit A hereto contains detail information of each sale including the sales price. The proceeds from these sales total approximately $18,970,798.00 million of which the Ratepayer Advocate is recommending that $12,987,908.00 million should go to ratepayers.[2] As shown on Exhibit B hereto, there are another seven (7) sales contemplated in the near future involving 266,892 square feet of office space that could result in additional proceeds of over $20 million.[3] Hence, the Board's decision in this matter is of great importance to the public interest and New Jersey ratepayers. All of the assets identified on both Exhibits A and B were placed in service while Verizon NJ was under rate of return regulation and were part of the rate base when the Board approved PAR-1.

As discussed further below, the Board has the inherent authority to direct that ratepayers share in the proceeds from the sale of assets as part of its specific statutory requirement to examine any disposition of utility assets under *N.J.S.A. 48:3-7, et. seq*.

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[2] The total on Exhibit A does not include the sale of property in Township of Brigantine.

[3] The Ratepayer Advocate notes that Verizon NJ filed on September 8, 2004 a petition to approve the sale of Real Property in Maplewood Township. See *I/M/O the Application of Verizon New Jersey Inc. for the Approval of the Sale and Conveyance of Real Property located in the Township of Maplewood, Essex County, New Jersey to 228 Burnett, L.L.C.*, BPU Docket No. TM04091019. This is one of the remaining seven properties shown on Exhibit B. The sales price is $3.3 million. The Ratepayer Advocate notes that the proceeds flowing to ratepayers from this sale based upon the journal entries filed with the petition and the Ratepayer Advocate's proposed treatment would amount to $2,378,634.41. The Ratepayer Advocate question the accuracy of the general entries since the building was constructed in 1975 and subsequent thereto an additional $3.6 million in other improvements were made. The depreciation shown on the journal entries may not be the total depreciation taken since the building was constructed in 1975. The property has been vacant since October of 2002. This case could have many of the same problems with improvements being made just prior to vacating the premises. This filing supports our claim that the proceeds from all seven properties could exceed $20 million.

The Board has exercised such authority in the past and has directed the sharing of proceeds with ratepayers.[4]

The instant investigation is intended to determine the extent to which New Jersey ratepayers will share in the direct financial benefit from the sale of Verizon NJ's assets, which assets ratepayers have financially supported since the assets became part of the utility's rate base. Despite two previous decisions not calling for sharing of proceeds from the sale of assets, the Board in the Plainfield-Hadley decision and order dated May 19, 2004, directed Verizon NJ to ensure that the proceeds from the transactions are available with interest in the event the Board decides that sharing the proceeds with ratepayers is appropriate. Indeed, the Board specifically held that this issue had not been specifically addressed as part of the PAR-2 proceeding and the subsequent Board Order in PAR –2.[5]

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[4] The Ratepayer Advocate notes that the Board handles sale of assets through two mechanisms. One is the ordinary course of business filing and the other is a formal petition which requires a Board order. The sales shown on Exhibit A are a mix of the two mechanisms. In the ordinary course of business sale under N.J.A.C. 14:1-5.6(d), a Secretary's letter is issued approving the sale. The Secretary's letter specifically reserves the right of the Board to revisit the sharing of proceeds with ratepayers. See Exhibit E, attached hereto which is copy of a Secretary's letter. The Ratepayer Advocate notes that *I/M/O the Application of Verizon New Jersey Inc. for the Approval of the Sale and Conveyance of Real Property in the City of East Orange, Essex County, New Jersey to Kenneth Esdale*, BPU Docket No. TM03050356, the Board issued a formal order even though the property qualifies for ordinary course of business treatment and approval through a Secretary's letter. The Board's Order of Approval dated July 9, 2004 lacks any direct statement that "Petitioner shall ensure that the proceeds from this transaction will be made available with interest at a rate to be determined by the Board in the event the Board ultimately determines that sharing of proceeds with ratepayers is appropriate." The subject order does contain the standard provision regarding journal entries which in the Ratepayer Advocate's opinion is sufficient to permit the Board to require sharing of the proceeds with ratepayers from this sale in the event the Board orders sharing with ratepayers in this ongoing investigation proceeding.

[5] See *I/M/O the Filing by Verizon New Jersey Inc. for the Approval of the Sale of Surplus Land to Plainfield-Hadley*, BPU Docket No. TM02050281, Order of Approval, dated May 19, 2004; *I/M/O the Board's Investigation as to Whether Ratepayers Should Share in the Proceeds Arising From the Sale and Conveyance of Real Property by Verizon New Jersey, Inc.*, BPU Docket No. TX04090749, Decision and Order, dated September 14, 2004; *I/M/O the Application of Verizon New Jersey, Inc. for the Approval of the Sale and Conveyance of Real Property Located in the City of Elizabeth, Union County, New Jersey to Kenneth Esdale*, BPU Docket No. TM04020105, Order of Approval, dated September 14, 2004.

The Ratepayer Advocate recommends that with respect to sale of telecommunication assets, the Board adopt a policy similar to that applied to other utility sale of assets and thereby permit New Jersey ratepayers to share in the financial proceeds generated when Verizon NJ sells utility assets that are no longer deemed used or useful to Verizon NJ's utility operations. Specifically, the Ratepayer Advocate submits that in the case of the sale of a non-depreciable telecommunication asset, i.e. land only, ratepayers should share with shareholders on a 50/50 basis, the net proceeds above the original cost and sales expenses [net proceeds = sale price less original cost and less sale expenses]. In the case of the sale of a depreciable telecommunication asset, i.e. land and improvements, the amount of the sale proceeds that recaptures depreciation previously taken by Verizon NJ would go 100% to ratepayers with 50/50 sharing above that amount. With this approach, there is no necessity to address what treatment would be appropriate, if there was an accounting loss. One would expect that the proceeds would not exceed the amount of the prior depreciation in a given case. Therefore, the entire proceeds would go to ratepayers.[6]

In the unlikely event, that the proceeds exceed the depreciation and there was a loss, the Board could address that issue on a case-by-case basis as part of the approval process. However, the Ratepayer Advocate does not support reducing the amount of proceeds available for sharing by losses on a sale. Each sale should stand on its own with no aggregating of individual sales. The Board should consider increasing the amount of proceeds available for sharing in a particular case to reflect a sharing of the tax benefits received from recording a loss.

[6] This recommendation is alternative recommendation to the Ratepayer Advocate's prior recommendation that 100% of the proceeds go to Access New Jersey to argument the equipment fund. The Ratepayer Advocate asks that the Board consider both alternatives as two separate recommendations.

The adoption of the above approach would in most cases eliminate the necessity to hold evidentiary hearings. However, in the appropriate case, the Board and/or the parties could request an evidentiary hearing. The Ratepayer Advocate applauds the Board's direction in its Decision and Order in *I/M/O Application of Verizon New Jersey Inc. for the Approval of the Sale and Conveyance of Real Property Located in the City of Elizabeth, Union County, New Jersey to Kenneth Esdale*, to examine the prudency of the Elizabeth's capital improvements made by Verizon NJ.[7] But, the Ratepayer Advocate recommends that the Board conduct such prudency proceeding in a separate proceeding apart from this investigation. Such separate proceeding would be a contested case with filing of testimony, discovery, and hearings with cross-examination. As discussed below, the scope of the separate proceeding should be expanded and include a review of earnings sharing under PAR-1.

BACKGROUND.

A. The Board Has The Inherent Authority And Has Traditionally Allowed Sharing Of Proceeds From Sales Of Utility Assets Among Shareholders And Ratepayers And Should Not Deviate From This Practice

The Board pursuant to *N.J.S.A.* 48:2-13 and *N.S.J.A.* 48:2-16 has the inherent statutory authority to review sale transactions of utility properties and to order sharing of proceeds between shareholders and ratepayers on the sale of utility property. Case law is replete with examples where the Court has upheld the Board's broad power to act under the Public Utility Law. The existence of and the reach of the Board's power was addressed in *Valley Road Sewerage Company*, 154 N.J. 224, 235-36 (1998). Judge

[7] *I/M/O Application of Verizon New Jersey Inc. for the Approval of the Sale and Conveyance of Real Property Located in the City of Elizabeth, Union County, New Jersey to Kenneth Esdale*, BPU Docket No. TM04020105, at page 4.

Pollock in delivering the opinion on behalf of the New Jersey Supreme Court stated that the New Jersey Legislature had vested the Board with "general supervision and regulation of and jurisdiction and control over all public utilities…and their property, property rights, equipment, facilities and franchises so far as may be necessary for the purpose of carrying out the provisions of [Title 48 of the New Jersey Statutes]."[8] The Court went on to further *emphasize* that "this sweeping grant of power is intended to delegate the widest range of regulatory power over utilities to the [BPU]."[9] The Court further observed that the "BPU's authority over utilities, like that of regulatory agencies generally, extends beyond the powers expressly granted by statute to include incidental powers that the agency needs to fulfill its statutory mandate." *Id.* at 236 [10] In *Valley Road Sewerage Company*, the Court upheld the power of the Board to revoke a water franchise even though no statute specifically authorized such action. *In Re Petition of New Jersey American Water Company*, 169 N.J 181 (2001), the New Jersey Supreme Court upheld the broad discretion of the Board in exercising its authority and further concluded that only in very rare situations will the Court not defer to Board's action under its deferential standard that presumes the validity of the Board's action. As noted *In Re Petition of New Jersey American Water Company*, the Court set aside the 50/50 sharing policy as it relates to recovery of such expenses in rates because charitable giving is unrelated to a

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[8] *N.J.S.A.* 48:2-13; See also, *Deptford Tp. V. Woodbury Terrace Sewerage Corp*., 54 N.J. 418, 424 (1969).

[9] The Court also found evidence of the BPU's wide grant of power under *N.J.S.A.* 48:2-40 *which provides that "the* BPU at any time may order a rehearing and extend, revoke or modify an order made by it." *Township of Deptford*, supra at 424-25; *See also*: *Valley Road Sewerage Company*, 154 N.J. 224, at 236-37.

[10] See also: *A.A. Masttrangelo, Inc. v. Commissioner of Dept. of Envtl. Protection*, 90 N.J. 666, 683-684 (1982); *New Jersey Guild of Hearing Aid Dispensers v. Long*, 75 N.J. 544, 562 (1978).

utility's core function.[11] It is clear that the assets at issue here are directly related to the core functions of providing telecommunication service because one of the findings is that such assets are no longer needed for utility purposes and they were originally added to the rate base. Therefore, the Board has the authority and discretion to require the sharing of the proceeds with ratepayers and that determination is presumptively valid under the deferential standard of review.

The Board is explicitly authorized to approve any sale or lease of utility assets under *N.J.S.A.* 48:3-7, which states the Board's authority to approve the sale, lease, mortgage, or other disposition of a utility's property. Similarly, the Board's rules in *N.J.A.C.* 14:1-5.6 set forth the filing requirements necessary to obtain Board approval of any sale or lease of utility property. Consistent with *N.J.A.C.* 14:1-1.2(a), the Board has the administrative discretion to liberally construe its rules to effectively carry out its statutory functions which includes conditioning the sale of any utility assets on the sharing of proceeds of such sale with ratepayers. Moreover, in practice, the Board has consistently and traditionally followed a long-standing policy and practice of allowing a sharing of proceeds from the sale of assets with ratepayers.

For more than twenty (20) years, the Board has ordered the sharing of the proceeds from sale of utility property with ratepayers. For example, in 2001, the Board approved a stipulation resulting in a 50-50 split between shareholders and ratepayers, on the net gain on sale of property totaling approximately $5.6 million which resulted in $2,838,159.00 due to ratepayers.[12] More recently in 2003, the Board again approved a 50-50 split

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[11] See *In Re Petition of New Jersey American Water Company*, 169 N.J 181, 196 (2001).

[12] See *In the consolidated matters of NUI Elizabeth Gas Company To (1) Revise Its Levelized Gas Adjustment Clause; (2) Review Its Existing Demand Side Management Adjustment Clause; And (3) Revise Its Rates For Commercial And Industrial Air Conditioning Service And Seasonal Delivery Service*, BPU

between ratepayers and shareholders of the proceeds from the sale of property sold for $1,543,200.00[13] As part of its order, the Board also found that it was appropriate to credit the company's MTC deferred balance upon closing of the transaction in the amount of $30,137.95 to compensate ratepayers for the benefit of three unexpired leases that would have benefited ratepayers had the property not sold. In yet another case in 2003, the Board upheld a stipulation resulting in a 58-42 split between shareholders and ratepayers respectively, resulting in a share of $495,930.00 due to ratepayers.[14]

Over twenty years ago, the Board again ordered sharing of proceeds from the sale of utility property in the Golf Course case,[15] wherein the Board approved a 50-50 split on the appreciated gain resulting from the sale, and further ordered a 50-50 split among ratepayers and shareholders of appreciated gain, if any, over and above the agreed upon fair market value of $23.8 million for a period of 15 years.[16] All these cases demonstrate that the Board has consistently ordered sharing with ratepayers with the percentage of

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Docket Nos. GR00070470 and GR00070471, *I/M/O NUI Elizabethtown Gas Company To Revise Its Weather Normalization Clause Rate*, BPU Docket No. GR00070483, and *I/M/O NUI Corporation For Authority Pursuant To N.J.S.A. 48:3-7 And N.J.A.C. 14:1-5.6 To Sell Certain Real Property In Woodbridge, New Jersey* ,BPU Docket No. GM00030158, and *I/M/O The Board's Review Of Energy And Home Heating Oil Markets*, BPU Docket No. GO00020088, Order dated September 26, 2001.

[13] See *I/M/O Jersey Central Power & Light For Approval Of The Sale Of Certain Property Situated In The Borough Of Hightstown, Middlesex County To Matthew And Suzette Lucas, H/W For $1,543,200*; BPU Docket No. EM02100799, Order dated October 10, 2003.

[14] *See I/M/O a Joint Petition By United Water-Lambertville, Inc., and Delaware & Raritan Greenway, Inc., For Approval Of The Sale Of Approximately 300 Acres Of Land Pursuant to N.J.A.C. Section 14:1-5.6*, BPU Docket No WM02080520, Order dated June 18, 2003,

[15] See *I/M/O Hackensack Water Company – Removal From Rate Base And Transfer Of Excess Lands; And Consideration Of Stipulation Regarding Golf Course Transfers And Utility Acquisition Watershed Properties*, BRC Docket Nos. 8312-1096, 8506-586, 8712-1465 and WC 90040266, BRC Order dated October 12, 1993.

[16] *See also, I/M/O Atlantic Sewerage Company for Authorization to Execute and Implement an Agreement of Sale*, BPU Docket No. WM98090790, wherein, the Board also order a sharing of profits with ratepayers, Order of Implementation, dated January 14, 1999.

sharing determined on a case-by-case basis. This is amply demonstrated in the sale of assets for electric utilities. The Board initially approved the use of a five (5) year net average of the gains after deducting any losses with 100% going to ratepayers and more recently in 2002 approved a 50-50 sharing of the five (5) year net savings.[17] What is clear from all these cases is that the Board will direct sharing when the underlying asset has been included in the rate base. In only two cases involving sale of property under PAR-1 has the Board declined to order sharing. In these two cases, the Board did in effect approve that 100% of the proceeds would be credited towards earnings for purposes of applying the earning sharing mechanism contained in PAR-1.[18] With the elimination of earnings sharing under PAR-2,[19] the mechanism is no longer available and as the Board recently recognized and acknowledged the Board's Decision and Order in PAR-2 did not specifically address what treatment is appropriate for the sale of assets.[20]

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[17] The Ratepayer Advocate has attached in Exhibit C hereto the pertinent portions of the Direct Testimony of Robert Henkes filed the recently Public Service Electric and Gas Company ("PSE&G") Case in BPU Docket ER02050303 wherein there is a full discussion of the Board's treatment of proceeds from the sale of assets as it relates to PSE&G.

[18] See *I/M/O the Application of Verizon New Jersey Inc. for Approval of the Sale, Lease or Lease Assignment of Certain of Its at 13 Locations in New Jersey to SBA Properties, Inc*., BPU Docket No. TM01090597, Order of Approval dated January 2, 2002, wherein the Board "Finds that the plan for Alternate Form of Regulation, pursuant to which Verizon is currently being regulated, provides the appropriate mechanism to share revenues between ratepayers and Verizon." See also *I/M/O the Application of Bell Atlantic-New Jersey, Inc. for Approval of the Sale and Conveyance of Real Property Located in the Township of Wall, Monmouth County, New Jersey to Florham Realty Group, Inc*., BPU Docket No. TM00020105, Order of Approval dated June 11, 2001, where in the Board "Finds that the plan for Alternate Form of Regulation, pursuant to which VNJ is currently being regulated, provides the appropriate mechanism to share revenues between ratepayers and VNJ."

[19] *I/M/O Application of Verizon New Jersey, Inc. For Approval (i) of a New Plan for an Alternative Form of Regulation, and (ii) to Reclasify Multi-Line Regulated Business Services as Competitive Services, and Compliance Filing ("PAR-2")*, BPU Docket No. TO01020095, Decision and Order, dated August 19, 2003.

[20] See *I/M/O the Filing by Verizon New Jersey Inc. for the Approval of the Sale of Surplus Land to Plainfield-Hadley*, BPU Docket No. TM02050281, Order of Approval, dated May 19, 2004; *I/M/O the Board's Investigation as to Whether Ratepayers Should Share in the Proceeds Arising From the Sale and Conveyance of Real Property by Verizon New Jersey, Inc*., BPU Docket No. TX04090749, Decision and Order, dated September 14, 2004; *I/M/O the Application of Verizon New Jersey, Inc. for the Approval of*

Similarly the Board has sanctioned the sharing of merger savings with ratepayers when companies have merged under its broad statutory authority granted under the Public Utility Law.[21] In such merger cases, the Board has paid particular attention to ensure that negotiated settlement proposals arrive at reasonable estimates of potential synergy savings associated with the merger and that those savings be allocated among companies and then between ratepayers and shareholders in a fair and equitable manner that ensures that New Jersey ratepayers receive a reasonable share.[22] In *First Energy*, the Board approved a stipulation that resulted in allocating a net present value of $400 million out of a total estimated $1.6 billion of merger savings to JCP&L with $300 million of that total going to New Jersey ratepayers. This holding follows a long line of cases where the Board approved the sharing of merger savings.[23] The Board has found sharing of merger savings to be appropriate in regard to telecommunications mergers involving Verizon NJ and it predecessor companies.

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the Sale and Conveyance of Real Property Located in the City of Elizabeth, Union County, New Jersey to Kenneth Esdale, BPU Docket No. TM04020105, Order of Approval, dated September 14, 2004.

21 Acquisitions of public utilities, i.e. mergers, are reviewed under *N.J.S.A. 48:2-51.1 et. seq*. The Board has also previously ruled on the propriety of ratepayer sharing in the financial benefits that flow there from.

22 See *I/M/O First Energy Corp. And Jersey Central Power And Light Company, D/B/A/ GPU Energy, For Approval Of A Change In Ownership And Acquisition Of Control Of A New Jersey Public Utility And Other Relief*, BPU Docket No. EM00110870; OAL Docket No. PUC 1585-01, dated October 9, 2001.

23 See */M/O/ Atlantic City Electric Company And Conectiv, Inc. For Approval Of A Change In Ownership And Control*, BPU Docket No. EM97020103, Order dated January 7, 1998, wherein the Board adopted an ALJ finding that 75 percent of merger savings attributable to Atlantic City Electric be allocated to the utility's ratepayers; See *I/M/O Atlantic City Electric Company, Conectiv Communications, Inc., And New RC, Inc., For Approval Of A Change In Ownership And Control*, BPU Docket No. EM01050308, Order dated June 19, 2002, wherein ACE agreed to reduce its Deferred balance by $30.5 million of such past deferred generation-related costs upon the closing of the merger and that ACE would write-off such amount effective as of the closing of the merger, resulting substantial savings and benefits to ratepayers.
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As part of its Decision and Order approving PAR-2 with modifications, the Board approved the sharing of merger savings with ratepayers by certain modifications to Life-Line and Access New Jersey. In reaching this decision, the Board did not make any specific factual finding that the earnings sharing threshold of PAR-1 was ever met or exceeded by Verizon NJ in relation to inclusion of merger savings for the periods PAR-1 was in effect. However, the Board recognized "…the fact that VNJ's PAR-1…[had] provided for a sharing mechanism, according to which earnings in excess of 13.7% would be shared with ratepayers.[24] The Board was also "…aware of the support of the Bell Operating Company in New Jersey by the State's ratepayers, which fact…justifies a sharing of Verizon merger savings with New Jersey ratepayers".[25]

It was the Board's stated belief, therefore, "…that a balanced approach, that would both allow a portion of merger savings to further fund [Lifeline and ANJ] and also provide closure to the long-standing controversy surrounding both the calculation of the savings derived from each of the mergers and the proper method of allocating some portion of those merger savings to New Jersey is in the best interests of the Company and its ratepayers".[26] Accordingly, the Board directed Verizon NJ to further fund the lifeline and ANJ programs under PAR-2.[27]

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[24] *I/M/O Application of Verizon New Jersey Inc. For Approval (i) of a New Plan for an Alternative Form of Regulation and (ii) to reclassify Multi-line Rate Regulated Business Services as Competitive Services, and Compliance fi*ling, BPU Docket No. TO01020095, Decision and Order (August 19, 2003) at 102. See Order, *I/M/O Board's review of the Amended and Restated Agreement and Plan of Merger Dated as of April 21, 1996 By and Between NYNEX Corporation and Bell Atlantic Corporation*, BPU Docket No. TM96070504, and Order, *I/M/O Joint Petition of Bell Atlantic Corporation and GTE Corporation for Approval of Agreement and Plan of Merger,* BPU Docket No. TM98101125 (March 15, 2000).

[25] *Id*.

[26] *Id*.

[27] *Id*. at 103.

The elimination of earnings sharing in PAR-2 did not preclude the Board from authorizing merger savings for the benefit of ratepayers. This coupled with the fact that the Board fully acknowledges that PAR-2 did not address whether proceeds from sale of assets should be shared with ratepayers, leaves the Board free to direct the sharing of proceeds from asset sales independently and separate from any PAR-2 requirements. Any Board direction to this effect is not a change in policy *per se* but a continuation of the long- standing policy on sharing proceeds from the sale of assets with ratepayers which flows directly from the elimination of the earning sharing mechanism of PAR-1. Verizon NJ has no basis to challenge, object, or request any adjustment under PAR-2.[28]

The Board properly concluded that it was lawful and appropriate for New Jersey ratepayers to receive a monetary beneficial share of savings emanating from the mergers with NYNEX and later with GTE. In this context, the Board rejected Verizon NJ's [then known as Bell Atlantic New Jersey] arguments regarding the Board's jurisdiction over the BA and NYNEX merger. The Board asserted its clear ability and obligation to assure that the merger would not prevent ratepayers from receiving safe, adequate, and proper service as provided for under Title 48.[29] In setting forth the issues to review in respect of the NYNEX merger, the Board declared it must be "…satisfied that the merger is

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[28] The Board's clarity on this point is demonstrated in its dispositions in the sale to Plainfield-Hadley. The Board's Order of May 19, 2004 required that the sale be completed by August 21, 2004 or the Board's approval would lapse, as well adding a caveat to ensure that the proceeds from the transaction would be available for distribution pending its decision in the instant matter. This result, after the applicable date of PAR-2, clearly enunciates the Board's acknowledgement that the issue of how ratepayers would share in the proceeds from the sale of Verizon NJ's utility assets had not been addressed in the PAR-2.

[29] *I/M/O Matter of the Board's Review of the Amended and Restated Agreement and Plan of Merger Dated as of April 21, 1996 by and Between NYNEX Corporation and Bell Atlantic Corporation; I/M/O The Board's Inquiry into Bell-Atlantic-New Jersey, Inc.'s Progress and Compliance with Opportunity New Jersey, its Network Modernization Program*, BPU Docket Nos. TM96070504 and TX96100707 (Order Dated January 23, 1997) at page 2.

consistent with law, that it will not cause economic or financial harm to ratepayers and that New Jersey ratepayers will have access to a share of any benefits relating to this merger".[30] The Board further noted that the Board's examination of the merger would take into account how the new Bell Atlantic quantifies and plans to share merger cost savings with ratepayers.[31] In its PAR-2 Decision and Order, the Board approved the sharing of merger savings from its examination of the contested savings associated with both the NYNEX and GTE mergers. As a result, the Board found that New Jersey ratepayers should receive their equitable share of the financial benefits generated by the respective mergers.

In view of the forgoing, there exist no reason why the Board should not follow its traditional policy and practice and order that proceeds from the sale of telecommunications assets should not be treated differently than the sales of other utility assets. This is particularly important when the assets sold were in fact included in the rate base. The Ratepayer Advocate submits that New Jersey ratepayers bore the financial burdens associated with the purchasing and placement of the assets into the rate base for which rates charged to ratepayers were predicated upon. Some of these assets have been in the rate base for close to five (5) decades and all these assets were in the rate base when Verizon NJ's predecessors were regulated under rate of return regulation. Verizon NJ and its predecessors bore no risk of loss during the regulated life of the assets. Sharing of the proceeds by ratepayers on sales of Verizon NJ's assets is just, reasonable, and equitable. To do otherwise, is just an unwarranted and improper windfall to Verizon NJ. The Ratepayer Advocate further opines that the elimination of the PAR-1 earnings

30 *Id*.

31 *Id*.

sharing mechanism in the PAR-2 proceeding and the failure of Verizon NJ to include a specific provision in PAR-2 addressing the sale of assets precludes Verizon NJ from objecting to any decision by the Board to allow a sharing of proceeds with ratepayers.[32]

In fact, the record in PAR-2 shows conclusively that Verizon NJ's justification for eliminating earning sharing makes no mention of sharing of proceeds from subsequent asset sales but instead focuses on elimination of the regulatory costs associated with monitoring earnings. See West Exhibit 4 that compares the provisions of PAR-1 with the Provisions of PAR-2 and West Exhibit 3, An Economic Appraisal of Earning Sharing" offered in support of the elimination of earnings sharing, attached hereto as Exhibit D.[33]

In West Exhibit 3, Verizon NJ argues that earnings sharing should be eliminated because "earning sharing mechanisms in price cap plans discourage investment, discourage efficiency, delay the offering of new services, promote the arbitrary allocation of costs, and lead to increased regulatory delays and regulatory costs." The Ratepayer Advocate notes that Verizon NJ stated reasons for elimination of earning sharing are contradicted by its subsequent actions in New Jersey. After being freed from earning sharing, Verizon NJ has refused to make investments in New Jersey for deployment of fiber to the premises because it dislikes the recent UNE rates set by the Board. This is nothing more than backsliding by Verizon NJ and reneging on its promise to increase investment. Additionally, Verizon NJ's parent is urging the elimination of the Board's

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[32] Even if Verizon NJ had included a provision in PAR-2 covering the sale of assets (which there is not), the Board is free under *N.J.S.A* 48:2-40 to change or modify any order, including its PAR-2 order. In such a case, Verizon NJ could only file a petition alleging an exogenous adjustment is warranted. The Ratepayer Advocate reserves its rights to contest whether any such filing would in fact qualify as an exogenous event and whether such event warrants any change in rates under PAR-2.

[33] West Exhibits 3 and 4 are exhibits to the Panel Testimony of Harold E. West, III and Dr. William E. Taylor, dated February 15, 2001. Exhibit 3 was prepared by Dr. Taylor and marked as West Exhibit 3.

authority to regulate Voice over Internet Protocol and elimination of the Board's authority to set intrastate rates under Section 271 of the Federal Telecommunications Act of 1996, all of which harms ratepayers. On top of all this, Verizon NJ wants to reap a windfall by not sharing the proceeds of assets sales with ratepayers. As a result, the Ratepayer Advocate urges the Board to reject Verizon NJ's call for not sharing proceeds from the sale of assets with ratepayers.

The fact that Verizon NJ is under an alternate form of regulation in PAR-2 does not affect or preclude the Board from directing sharing of proceeds from the sale of assets. The Ratepayer Advocate urges the Board to following the reasoning of the New York Public Service Commission in *Bellcore*.[34] As previously set forth in prior comments to the Board, the Ratepayer Advocate submits that it was proper for the NYPSC to direct that the profits from the sale of Bellcore by New York Telephone ("NYT") be passed on to ratepayers because NYT's interest in Bellcore had been funded through payments from ratepayers.[35] The New York Court of Appeals' analysis is reasonable and proper for application here in New Jersey. In rejecting the argument that only shareholders have borne the risk of loss, the Court of Appeals highlighted the reality that "…in fully funding the Bellcore investment through telephone rates, NYT's customers effectively eliminated that risk, guaranteed the maintenance of Bellcore's value and funded Bellcore dividends to shareholders.[36] New Jersey ratepayers, likewise, have financially sustained

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[34] See *I/M/O New York Telephone Company v. Public Service Commission of the State of New York, et. als* 95 N.Y. 2d. 40, 731 N.E.2d 1113, 710 N.Y.S. 2d 305 (2000) at 307, 309 ("*Bellcore*").

[35] *Id*. at 307.

[36] *Id*. at 310. The Court of Appeals cited to *Democratic Central Committee v. Washington Metro. Area Tr. Commn*, 485 F. 2d. 786 at 806 ["an investor can hardly muster any equitable support for a claim to appreciation in asset value where he has been shielded against the risk or loss on investment, or has already been rewarded for taking on that risk"].

the development and growth of the utility property Verizon NJ now wants to shed from its operations. Consistent with the reasoning offered by the Court in *Bellcore*, New Jersey ratepayers have eliminated the investment risk of shareholders, funded shareholder dividends, and bolstered the value of the company on the whole. The Ratepayer Advocate asks that the Board follow the approach by the NYPSC as it is just, reasonable and proper.

As the New York Court of Appeals stated:

> "In our judgment, the PCS's justification, based on ratepayer's funding of NYT's interest in Bellcore, affords a rational basis… because NYT's customers bore the costs of creating the intrastate portion of Bellcore's value, they are entitled to reap the corresponding share of NYT's gains on the sale of Bellcore". *Bellcore*, at 310.

Accordingly, the Ratepayer Advocate submits that the Board follows *Bellcore* here in New Jersey.

The Ratepayer Advocate Recommends the following Approach in Sharing Proceeds from the Sale of Assets.

In determining what portion of the proceeds from sale of assets should be shared from the sale of assets, the Ratepayer Advocate recommends that the Board distinguish between non-depreciable assets and depreciable assets as follows:

1) non-depreciable assets: such as land

the acquisition cost shown on the utility's books;
plus (+) the sales related expenses;
minus (-) the purchase price of assets = (Net Proceeds)

On non-depreciable assets, the Ratepayer Advocate recommends a sharing of the "net-proceeds" on a 50-50 basis between shareholders and ratepayers.

2) depreciable assets: such as real property with improvements

On depreciable assets, the Ratepayer Advocate recommends that the proceeds of sale go 100% to ratepayers to the point where prior depreciation has been fully

recaptured. Thereafter, where proceeds exceed the prior depreciation, the Ratepayer Advocate recommends that the remaining proceeds of sale be split on a 50-50 basis between shareholders and ratepayers.

To illustrate the Ratepayer Advocate's recommendation, we ask that the Board consider the following example:

> **Sale of depreciable asset has a book value of $1.5 million with a sale price of $10 million. If $3.5 million has been taken in depreciation (assuming an initial purchase price of $5.0 million, then the first 3.5 million go fully to ratepayers and the remainder $ 5.0 million ($10 million minus $3.5 million minus $1.5 million = $5.0 million) is split on a 50-50 between shareholders and ratepayers.**

The Ratepayer Advocate opines that this recommended approach will avoid having to determine what treatment the Board should apply to what might appear as a loss under accounting rules, since regardless of whatever treatment a company wishes to employ on its books for accounting and/or tax purposes, an asset sold at a loss will have prior depreciation which in most cases would not exceed the proceeds of the sale, 100% would go to ratepayers and any excess over the prior depreciation would be a loss and only the tax benefit would be available to be apportioned as directed by the Board. The Ratepayer Advocate recommends that the Board should decline to permit any reduction in the amount of the proceeds to be shared to account for losses on sale of assets. However, the Ratepayer Advocate would support increasing the amount of proceeds to be shared to reflect the tax benefits from a sale of an asset at a loss.

The Board Has the Inherent Authority To And Should Order Hearings When Issues of Prudency Arise From the Sale, Purchase, or Lease of Assets by Utilities.

In the ultimate analysis, a utility company whether it be a water, gas, electric or telecommunications company, is subject to having its transaction reviewed for prudency and reasonableness. As discussed above, the Board has been entrusted with broad

inherent authority, under *N.J.S.A.* 48:2-13, and *N.J.S.A.* 2-16 to oversee that the actions of a utility company and whether its actions and conduct are prudent and reasonable.

The Ratepayer Advocate supports the Board's decision to examine the prudency of the improvements made to the Elizabeth property by Verizon NJ.[37] Such examination should be conducted as a contested case with notice and hearings, including discovery, filing of testimony, and hearings with cross-examination. In particular, the Ratepayer Advocate submits that a contested case procedure is warranted because of the four (4) separate journal entries and the various discrepancies related to each entry that were submitted during the Esdale proceeding. Substantial prudency issues are implicated by the mere fact that improvements totaling in excess of approximately $2 million were made to the property before the property was vacated and subsequently put up for sale and by Verizon NJ"s decision to abandoned newly improved property and incur substantial long term lease expenses.

Similarly, the Ratepayer Advocate would recommend that as part of any prudency proceeding, the Board include in such proceeding other situations where substantial improvements have been made and the property is subsequently vacated and sold. One such example, is a recently filed petition dealing with property located in the Township of Maplewood.[38] In Maplewood, according to the petition, Verizon NJ made capital improvements totaling $3,681,204.00 after the building was built in 1975. Verizon NJ provides no details as to when such additional improvements were made. This raises the

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[37] See footnote 7 above; *I/M/O the Board's Investigation as to Whether Ratepayers Should Share in the Proceeds Arising from the Sale and Conveyance of Real Property by Verizon New Jersey, Inc.* BPU Docket No. TX04080749, Decision and Order, dated September 14, 2004.

[38] *I/M/O the Application of Verizon New Jersey, Inc., for the Approval of the Sale and Conveyance of Real Property Located in the City of Maplewood, Essex* County, *New Jersey to 228 Burnet L.L.C*., BPU Docket No. TM04091019.

same concerns that exist with the City of Elizabeth, the Esdale, sale. The Ratepayer Advocate notes that if after review by the Board, any expenses are found to be imprudent, then such findings could affect earnings sharing under PAR-1. Therefore, the Ratepayer Advocate would recommend that the Board as part of its prudency review, conduct an full and complete review of earnings sharing under PAR-1 to ensure proper accounting of revenues, expenses, and other matters that affect earnings sharing under PAR-1. In addition, the Ratepayer Advocate requests that the Board review whether the rate base (which is a component for application of the earning sharing mechanism) reflects appropriate adjustments arising from the reclassification of services, retirement of items from the rate base and other appropriate adjustments during PAR-1.

By way of example, under the Stipulation and Agreement of Settlement in the payphone proceedings,[39] various revisions to revenues and expenses for the period covered by PAR-1 are to be made.[40] In addition, under the two sale of assets cases identified in footnote 18, above, wherein the Board held that the revenues from sale of such assets would be factored in to the earning sharing mechanism under PAR-1, the Board should review whether Verizon NJ actually made adjustments to reflect increased revenue from these sales. It would also be appropriate to review whether revenues from

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39 See *I/M/O the Petition of Bell Atlantic-New Jersey for an Order Finding That Petitioner BA-NJ's Pay Phone Operations Are Not Subsidized By Exchange Or Exchange Access Services* – BPU Docket No. TO97100792; *I/M/O the Filing by Bell Atlantic-New Jersey, Inc. Tariff Revision, Dkt. No. TT97010016; I/M/O Petition of Bell Atlantic - New Jersey to Discontinue Limited Inter Lata Dialing (LID) feature in Customer Provide Pay Phone Service Tariff (CPPTS) and to decrease rate for the Line Side Supervision Feature in the CPPTS Tariff*, BPU Docket No. TT97050360; *I/M/O the Filing By The New Jersey Pay Phone Association For Board Approval of Certain Competitive Pay Phone Issues*, BPU Docket No. TO92121070; The Stipulation and Agreement of Settlement covering the above referenced proceedings approved by the Board in its Telecommunications Order Approving Partial Initial Decision Settlement, dated October 24, 2000.

40 See paragraphs 7, 9, and 10 of the Stipulation and Agreement of Settlement.

sales in the ordinary course of business have been properly reflected in revenues during PAR-1. Furthermore, the Ratepayer Advocate submits that reported revenues under PAR-1 should be adjusted (increased) to impute additional revenue resulting from the change in classification of an exchange area that would have occurred if Verizon NJ had followed Section 5.1.2(B) of its Tariff B.P.U.- N.J. No. 2, Exchange and Network Services. In that regard, the Ratepayer Advocate notes that Verizon NJ has filed a petition asking for exchange area reclassification under PAR-2.[41] Verizon NJ apparently believes such adjustments are not precluded by the terms of PAR-2. Therefore, the Ratepayer Advocate submits that Verizon NJ similarly has the same belief for PAR-1 and the rate caps of PAR-1 did not preclude adjustments during the period of PAR-1. Verizon NJ's failure to effectuate such adjustments results in the understatement of revenues that should be reflected in the earnings sharing calculations under PAR-1.

In conclusion, the Ratepayer Advocate recommends the following to the Board:

- The Board requires the sharing of proceeds from the sale of telecommunication utility assets with ratepayers.
- The Board adopts the Ratepayer Advocates recommendation for 50/50 sharing of proceeds from the sale of non-depreciable assets and for depreciable assets, 100% of the proceeds going to ratepayers until the previously taken depreciation is recaptured and thereafter any excess proceeds are shared 50/50.
- The Board address sale of assets on a case-by-case basis and decline to net losses against gains, but increase the proceeds available for sharing by sharing the tax benefit received from a loss on a 50/50 basis with ratepayers.
- The Board conducts a prudency review of the improvements made to Verizon NJ's property in the City of Elizabeth and other similar transactions, but conduct

[41] See. *I/M/O Filing by Verizon New Jersey Inc., of a Revision of Tariff B.P.U.-N.J. No. 2, as Listed in Appendices, Providing for a Revenue Neutral Rate Restructuring Including a Restructure of Residence and Business Basic Exchange Service and Elimination of $0.65 Monthly Credit*, BPU Docket No.TT04060442, filed June 16, 2004.

such proceeding in a separate proceeding from this investigation as a contested case with evidentiary hearings.

- As part of the prudency proceeding, the Board conduct a full and complete review of earnings sharing under PAR-1 to ensure the proper accounting of revenues, expenses, rate base adjustments, and other matters that affect earning sharing under PAR-1.

Very truly yours,

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Service List.