

system because it distributes the burden of funding the universal service subsidy across an extremely broad base of telecommunications users. It has also proven extremely easy to administer. Those customers receiving benefit from the network provide the revenue stream for the subsidy.

Currently, the CHCF funds mostly the small LECs that serve high cost areas. Other high cost areas are funded through implicit subsidies in local exchange carrier rates. Pacific and GTEC have a number of exchanges which may be considered high cost once the implicit subsidies are made explicit. Although the Commission will not know the size of the subsidy needed to support universal service until cost studies for the GSAs are analyzed, funding needs for high cost areas could certainly be larger than the current size of the CHCF.

**b. Positions of the Parties**

GTEC, Pacific and the small LECs support an AEUS. The Coalition believes that it is premature for the Commission to determine a funding mechanism because it is not known whether residential basic exchange service is in fact subsidized and if so, by how much.

McCaw believes that a general tax to support universal service would be the most efficient and broad-based source of universal service funding. In the absence of such a tax, McCaw contends that a surcharge based on an equal charge per access line, customers or minutes of use would be more competitively neutral than a surcharge based on billings.

TET suggests that the current funding mechanism be updated and expanded to include revenue streams from end users as well as all providers.

The City of Los Angeles believes that there must be a fair and reasonable apportionment of cost between telecommunication providers and users. All telecommunication providers should contribute in order to promote fair competition in the marketplace.

AirTouch argues that cellular carriers should not be required to support universal service funds. AirTouch maintains that since wireless service is not an essential service it should not fund universal service.

TURN believes that a high cost fund should be funded from carrier contributions, and not from an AEUS. TURN argues that the new funding mechanism for high cost areas be based on net common carrier revenues. A carrier's net common carrier revenues equals its common carrier revenues reduced by payments made for telecommunications services that have already been subjected to the fund assessment. TURN's proposal is based on the net trans account idea developed by Eli Noam of Columbia University.

Under Noam's system, an independent administrator sets up a universal service account for each carrier. Under the net trans account, all carriers that provide transmission path services to third parties for compensation are included in the system. This includes all facilities-based two-way transmission carriers: the LECs, interexchange carriers (IECs), cellular carriers, competitive access providers, and private microwave and satellite carriers.

The administrator debits carriers a flat percentage of their transmission path revenues, net of transmission charges paid to other carriers. The administrator calculates the transmission path revenues by summing revenues from local service, intraLATA toll, interLATA toll, mobile telephone calls, access, interconnection and collocation payments received, reseller payments, private lines and high-capacity business services, transmission services for information providers, packet switched transmission services, transmission parts of integrated systems packages, basic Centrex services, and central office switching functions. From this total, the administrator subtracts the transmission charges that carriers have paid to other carriers. For example if an IEC has paid an LEC access charges, the total of

those charges is subtracted from the IEC's transmission path revenues. The administrator then credits carriers for their universal service contributions and for subsidized users choosing the carriers' service.

Noam points out that some carriers, with the exception of the large LECs, are not currently required to keep accounting records which will identify specific transmission path revenues. Noam also points out that the system may be subverted if the net trans account is only implemented in a few states.

TURN contends that this type of funding mechanism has the following advantages: (1) unnecessary transfers of monies will result because carriers can offset their contributions to the fund with expected monies from the fund; (2) it eliminates the incentives to price discriminate because the raising and lowering of rates to reflect payment of and receipt of monies from the fund, respectively, is eliminated; (3) it provides incentives for carriers to serve areas of the state where subsidies are available because it will reduce the monies the carrier needs to contribute to the fund; (4) it allows the funding to be spread over a number of providers subject to the mechanism, which minimizes the net impacts on customers; (5) if an AEUS is used, an incorrect price signal may be sent to consumers if the AEUS is increased; and (6) all telecommunication providers should contribute to this fund because their networks are enhanced when all customers have the ability to make and receive telephone calls from their home.

**c. Discussion**

The AEUS system has advantages and disadvantages. One advantage is that the basis of an AEUS system is already in place, and is easy to administer. Once the Commission knows the subsidy amount needed it will not be difficult to calculate the AEUS percentage for funding high cost areas. Carriers simply charge end users based on a percentage of the amount of telecommunications services they use. Another advantage is that the AEUS is effective

in showing the explicit amount of subsidy necessary to fund universal service. End users would see that they are paying a certain percentage of their bills to keep basic service rates affordable in high cost areas.

The AEUS also has its disadvantages. With the AEUS, the entire cost of the subsidy is shifted to end users. Another disadvantage is that the AEUS may be viewed as a tax on telecommunications services to support basic service in high cost areas. If the funding needs for high cost areas increase dramatically, customers may see a large jump in this surcharge.

The net trans concept has several advantages. It bills carriers, not end users, and therefore may not be perceived as a tax by consumers. The system also considers universal service contributions before billing carriers so that money transfers are minimized.

The net trans account also has some potential disadvantages. New accounting systems would have to be put into place to track transmission path revenues. It might also lead to some gaming as to what kinds of services are considered to be transmission. Such a charge might also affect a provider's choice of how information should be transmitted. The net trans account might also lead to problems in deciding what kind of technology providers should be subject to the net trans charge.

The Commission is undecided at the moment whether a funding mechanism based on the net trans account system is preferable over the AEUS. Although proposed Rule 6.F. sets forth a net trans account, we emphasize that we are still undecided whether the net trans account or the AEUS should be used.

We request that parties comment on the possible problems noted by Noam: (1) whether the net trans account will result in a burden on some carriers because they will have to track their transmission path revenues; and (2) whether the system will work if it is implemented in California, but not in other states. We also solicit additional comment on our concerns about the net trans concept, and what can be done to address those concerns.

If the net trans account is adopted, we propose that all telecommunication service providers subject to our jurisdiction be required to contribute.

Any universal service funding plan requires a funding administrator, who is responsible for collecting and depositing contributions into the fund, and for disbursing the money to the appropriate carriers. These duties are similar to those currently required to administer the ULTS fund and the CHCF.

Some of the commenting parties suggest that a neutral fund administrator be selected. Others suggest that the Commission act as the fund administrator.

If the funding administrator is a neutral third party, the Commission would have to select the administrator, and monitor the activities of the administrator and the carriers paying into the fund and receiving monies from the fund. In addition, administrative fees to the administrator would have to be paid, which would result in an additional charge. If necessary, the neutral third party might have to request the Commission to conduct audits or engage in other investigative activities to ensure the following: that the carriers are paying their share; and that carrier fraud can be detected.

We are inclined at the moment to have the Commission itself administer the high cost voucher fund mechanism. Such a proposal will eliminate the need to pay an administrative fee to the administrator. It also allows for easier enforcement of the fund in the event carrier revenues need to be audited, or if a

carrier's certificate of public convenience and necessity needs to be revoked for failure to pay its share into the fund. (See proposed Rule 6.F.4., App. A.) We invite further comment on whether the Commission should administer the fund or if a third party with fund management experience should administer the fund. We are particularly interested in receiving comments about the resulting delays and administrative difficulties the Commission might encounter in conducting audits and investigations, or revocations, if the administration of the fund was left up to a third party.

**D. The Mechanism for Funding Low Income Customers**

The current mechanism for funding low income customers is the ULTS program. Under the ULTS program all LECs throughout the state charge residential low income customers an installation charge of \$10.00,<sup>28</sup> and a monthly fee of \$5.62 for flat rate service or \$3.00 for measured service. Each LEC is then allowed to draw money from the ULTS fund which covers the difference between the statewide ULTS rate and the carrier's rate for residential basic service, as well as for certain expenses associated with the program. However, the residential basic service rates differ depending on the LEC, and consequently so does the subsidy amount. For example, Pacific, which serves 79% of the access lines in the state, has a residential flat rate of \$11.25. Pacific draws \$5.63 per ULTS customer on a flat rate. GTEC, the state's second largest LEC, has a residential flat rate of \$17.25. GTEC draws \$11.63 per ULTS customer on a flat rate. The rest of the LECs' rates vary, but they cannot exceed 150%.

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<sup>28</sup> The ULTS installation charge for some of the small LECs is less than \$10 because of the restrictions contained within PU Code § 874(c).

All of the parties commenting on this issue agree that with the advent of local exchange competition, the Commission needs to revise the ULTS program so that all carriers providing basic exchange service to low income customers can avail themselves of the ULTS fund or a variant of that fund.

In contrast to the likelihood that funding needs for high cost areas are likely to increase, it is not expected that the funding level for ULTS will increase significantly. We propose that the existing ULTS program remain in place as we move toward markets with multiple providers. However, the ULTS program needs to be modified so that the subsidy will be available to those local exchange providers who serve low income customers with basic exchange services. (See proposed Rule 5.A.1., App. A.) It may be necessary to reopen the ULTS proceedings to make some necessary changes to the existing ULTS program.

With competition in the local exchange, we believe that a virtual voucher system for ULTS customers, similar to the virtual voucher for high cost areas, will help to eliminate customer confusion. Under the virtual voucher approach, the ULTS customer only needs to choose a provider of local exchange service. The local exchange provider may not charge a ULTS customer any more than the statewide ULTS rate as determined by the Commission pursuant to PU Code § 879. The provider of the service must then manage the customer account to access subsidy funds with the ULTS voucher. Customers will see the subsidy from the ULTS program on their monthly bills. With a ULTS virtual voucher, income eligible customers will benefit by having greater choice over their local exchange provider. To ensure the competitive neutrality of this low income customer subsidy, the CLC should not be allowed to collect a subsidy in excess of what the incumbent LEC receives on a per customer basis. (See proposed Rule 5.A.1.C., App. A.)

To ensure that the universal service goal of providing affordable service is continued in an era of local exchange

competition, we propose that all local exchange providers be required to inform prospective customers upon the initiation of service that a ULTS rate is available if the customer meets the ULTS income qualifications. They will also be required to keep track of the number of customers who sign up each month for the ULTS program. Such information shall be submitted to CACD's Telecommunications Branch on a monthly basis. (See proposed Rule 5, App. A.)

During this transition to open competition, the Commission plans to follow the state mandated ULTS rates provided for in PU Code § 874. If competition drives the price of basic exchange service down, the Legislature may wish to revisit whether the rates provided for in PU Code § 874 need revision. In the long run, competition and technological advancements may eliminate the need for a ULTS program altogether. The Legislature and the Commission may want to review in a few years how effective and necessary the mandates contained in the Universal Telephone Service Act (PU Code § 871 et seq.) are in a competitive environment.

The Commission believes that the current AEUS for funding the ULTS program has worked and will continue to work once we open the local exchange to competition. We propose to maintain the AEUS for the ULTS program. All providers of local exchange service will be required to charge the appropriate surcharge on all end users of telecommunications services except for ULTS customers.

DCA states that the current self-certification process for the ULTS program should be changed to meet the federal verification standards. By changing the current certification process, DCA contends that the Commission could reduce the amount of the ULTS subsidy because California would be eligible to double its level of federal lifeline funding. The potential offset could be used to help fund telecommunications and information infrastructures for public schools and libraries.

With competition, there will soon be more providers offering basic service under the ULTS program. It may be beneficial to change the self certification program to an income verification program that meets federal guidelines so that uniform eligibility requirements are followed, and potential fraud is eliminated. By doing so, more monies from the federal lifeline program should be available. A potential disadvantage is that additional ULTS program costs may be incurred by the providers to verify that the customer is indeed eligible for the ULTS program. Parties are invited to comment on whether the Commission should change from a self certification program to an income verification program, and whether these additional funds could be used for public schools and libraries.

We welcome comment as to whether our proposed changes to the ULTS program are responsive to the changes taking place in the local exchange markets. We also request comment on whether the Commission or a third party should act as the fund administrator for the ULTS program. Also, we request comment on whether a revised ULTS program should be adopted and implemented before the high cost voucher fund is adopted.

## VII. Consumer Information

### A. Introduction

In the universal service OIR/OII, the Commission requested comment on consumer information issues that arise in connection with universal service.<sup>29</sup> The Commission wants to ensure that consumers have a sufficient amount of information

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<sup>29</sup> Consumer information issues need to be distinguished from consumer protection issues. The latter are being addressed in the Local Competition OIR/OII.

available to them so that consumers can make informed choices about their telecommunications provider and available services.

At the current time, PU Code § 786 requires that on or before March 1st of every year, every telephone corporation operating in the state provide to each residential customer a list of the residential telephone services that it provides, the rates or charges for those services, and the state or federal agencies responsible for regulation of those services.

**B. Positions of the Parties**

The parties who commented on what type of consumer information should be made available, and who should prepare and make the information available, represent three different points of view. The first view is that the Commission should take a hands off approach and allow the marketplace to dictate what sort of consumer information is needed. This view also recognizes that some minimum level of required information may be necessary.

The smaller LECs are of the view that no requirements other than compliance with PU Code § 786 are required. Their service territories are small enough in size that communicating with their customers is not a problem.

The third view, which is supported by Citizens, the Coalition, DCA, DRA, Public Advocates, TURN, and UCAN believes that the Commission may need to prepare and distribute some consumer information. Citizens states that the Commission should work with other public service agencies to provide information on the availability of subsidy programs to eligible customers, and that the Commission needs to respond to complaints regarding the dissemination of inaccurate or misleading information.

The Coalition believes that carriers should be required to provide specific information about residential service, and that a chart of the services and rates offered by carriers offering basic exchange service should be developed.

DRA believes that with open competition, the Commission will not have the resources to police all the information that will be provided to the public. DRA states that the information disseminated to the public must conform with the filed and effective tariffs. DRA also recommends that the Commission prepare an annual comparison, available upon request by consumers, comparing and describing the basic universal service rates and charges of LECs and large CLCs. Information regarding service complaints that the Commission has received should also be included in the comparison.

Public Advocates believes that the Commission needs to be in a position to respond promptly to complaints about marketing abuses and misinformation, and that complaints be rapidly investigated and resolved. They also believe that consumers need more information on special services and programs, and on billing disputes.

TURN supports the Coalition's proposal for rate information about basic exchange services being presented in a standardized format. In addition, TURN suggests that the Commission explore the possibility of requiring a similar matrix for toll services.

UCAN states that in order for universal service goals to be met, and for an effective competitive market to evolve, consumers must have access to price and service information which is relevant and presented in an easily understood format. Such a requirement will enable consumers to understand and effectively compare the new services and rates which will be available to them. UCAN says that the carriers should also be required to inform customers about how customer information is handled, and under what circumstances such information might be disclosed. This type of information should be made available to all consumers, regardless of income level, geographic location or language.

UCAN suggests that the preparation and dissemination of this information be the responsibility of the carriers, but that it be supervised by the Commission and independent consumer groups. UCAN envisions that rate information will be distributed by both the carrier and the Commission. The Commission's rate information would offer rate information relating to all carriers, as well as information on selecting a carrier or how to best shop for services.

UCAN also proposes that the Commission or a neutral third party compile information relating to complaints, and that the information be made available to consumers upon request. UCAN says that carriers should be required to include a notice about the availability of this information.

### C. Discussion

With the opening of the local exchange markets to competition, we believe that residential consumers should have information available to them which allows for an easy comparison of rates. Such information will help to make our regulatory changes more understandable to the public, and allow customers to make timely and informed choices without resulting in a burden on the carriers so as to discourage competition.

We propose that the idea of a matrix of certain required information regarding basic exchange services be available to consumers in any marketing information that targets residential customers and explains the telecommunication service offerings available. Proposed Rule 7 reflects the kind of information that is required. This matrix may be contained within other marketing information. However, the matrix of required information shall be set apart from the other marketing information with the following statement: "The following information is required by the California Public Utilities Commission to allow comparisons with rates charged by other providers for the same type of service."

No review or approval of the matrix is required. Commission review and approval of consumer information could delay provision of timely and accurate information, while creating an additional burden for regulators. However, if abuses or misinformation occur with respect to the matrix information, the Commission will investigate as is necessary, and impose substantial penalties.<sup>30</sup>

We do not believe that it is necessary for the Commission to mandate the provision of other consumer related information at this time.

With respect to potential barriers which may prevent certain segments of the population from obtaining consumer information, both Pacific and GTEC are undertaking efforts to target non-English speakers with information about their services. We expect that trend to continue. (See D.94-09-065, pp. 272-279.) As rates move toward costs, and subsidies become more targeted, competitive pressures should force all carriers to actively compete for business from all segments of the population. The requirements imposed on GTEC and Pacific in D.94-09-065 should continue to apply so long as they retain market power.

Although we do not propose to impose the same sort of reports and marketing plans on the CLCs and the other incumbent LECs at this time, we believe that all carriers providing local exchange service should strive to achieve our universal service goal of at least 95% for every segment of the population in California. As part of the required annual reports, we propose to adopt the DCA suggestion that the CLCs and the incumbent LECs, except for Pacific and GTEC who have their own reporting

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<sup>30</sup> The Legislature should consider amending PU Code § 2107 to increase the penalty amounts. The present penalty schedule may not act as a sufficient deterrent when sums much greater than the penalty amount are at stake.

requirements, report on their efforts to attain this goal for non-English speaking and low income people in the communities that these local exchange providers serve. (See proposed Rule 3.B.3., App. A.) As noted earlier, the penetration rates could reflect on the carrier's ability to become a designated COLR in high cost areas. This reporting requirement is transitional in nature, and may be eliminated after the markets become competitive.

### VIII. Recovery of LEC's Investment

#### A. Introduction

Most of the incumbent LECs contend that they must be compensated for their unrecovered network investment. The LECs assert that those investments were made under the existing regulatory structure with the expectation that they could recover those costs, an expectation not guaranteed by the competitive marketplace.

#### B. Position of the Parties

GTEC contends that as part of the new universal service policy, there should be a transitional program to amortize embedded investments placed by the LECs to meet past COLR obligations. According to GTEC, the LECs have been required to make those investments in the past to meet their service obligations. To the extent that the LEC's embedded investment has not been amortized over time at rates matching their economic lives, some portion of the LEC's current cost levels represents the cost of past obligations that were required by policymakers to provide universal service. GTEC proposes a transitional program that is separate from the funding for ongoing COLR obligations.

Pacific also contends that incumbent LECs must be compensated for their unrecovered network investment if they are displaced as the existing COLR. According to Pacific, this investment was part of a regulatory compact made before competition

was allowed, and that such investment was dictated by the Commission to ensure reliable, high quality telephone service by a single provider. Pacific proposes that it be allowed to amortize the amount of under recovered capital over a period of five years. Pacific recommends that a broad billing surcharge on all providers is an appropriate recovery mechanism.

Roseville also believes that the LECs should be permitted to recover the embedded costs of facilities required to extend service in the past to all in their territories as well as the ongoing costs of providing universal network access to all subscribers in their territories in the future. Roseville contends that the situation is analogous to the electric industry where the Commission has recognized the need to compensate utilities for investments made in the past that may be uneconomic in a competitive environment.

The Coalition argues that the gradual growth of competition will mean there will be no stranded investment for incumbent LECs. The Coalition notes that substantial barriers exist which will prevent new entrants from obtaining a large share of the market soon. The Coalition further contends that increases in demand may compensate for loss of market share as has occurred in the long distance market. The Coalition also argues that some degree of stranded investment is a natural consequence of competition and that the LECs' shareholders should bear some of those costs.

### C. Discussion

We do not believe that the LECs should be granted any additional recovery for stranded investments. Rate of return recovery is based on traditional rate of return ratemaking. We have been moving away from that concept since 1989.

The NRF decision in 1989 transformed the regulatory compact for Pacific and GTEC. The incentive-based regulatory framework was intended to expose shareholders to the risk

associated with investments in order to provide an incentive for more efficient investment. In D.89-10-031 the Commission determined that it would not entertain applications by GTEC or Pacific seeking ratemaking adjustments to account for changes in depreciation practices. (33 CPUC2d at p. 217, FOF 53.)

D.89-10-031 (33 CPUC2d 43) explicitly sought to disassociate rates from depreciation schedules, and force utilities to treat depreciation rates as firms in competitive markets would.

NRF also signalled the gradual expansion of competition. The problem that GTEC and Pacific raise of excessive amortization periods has been diminishing as the expected life for depreciation purposes has been steadily reduced. Moreover, investments made in anticipation of competition should not be regarded as stranded investment.

There are also substantial differences between the electric and telephone industries which justify differing treatment of stranded investment. Electric generation is characterized by large capital investments. In the electric industry, stranded investments are those generating assets that are demonstrably uneconomic, i.e., the cost of procuring energy from these sources is higher than others in the electricity market. The telecommunications industry, on the other hand, is characterized by smaller investments, and more frequent replacements as technology changes.

Finally, there is no reason to believe that the incumbent LECs will have substantial stranded investments due to their past obligation to serve. According to their own representations, LECs' obligations are primarily due to serving high cost areas where competitors will be reluctant to enter. The assets associated with serving the high cost areas will not be stranded if the incumbent LEC continues to serve the high cost area, or if it resells its facilities to other providers.

### IX. Procedural Process

As indicated earlier, it may be necessary for the Commission to issue one or more interim decisions regarding the issues surrounding universal service before a final set of universal service rules are adopted. This is necessitated by the interrelationship of issues such as cost studies with other Commission proceedings, the overall scheduling of other proceedings, and our intent to open all markets to competition by January 1, 1997. To achieve that goal, the following procedural schedule will be followed for this proceeding.

Interested parties will be allowed to file opening comments to the proposed universal service rules on or before September 1, 1995.<sup>31</sup> The Commission will hold a full panel hearing in connection with this proceeding on September 29, 1995 beginning at 9:00 a.m. in San Francisco.

Public participation hearings (PPHs) will be held at different locations throughout the state in the September and October timeframe regarding the proposed rules. The tentative locations and dates are listed below. These dates and locations may be changed, if needed, by the Assigned Commissioner. A ruling will be issued by the Assigned Commissioner in the near future confirming the locations and dates of the PPHs.

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<sup>31</sup> In the ALJ ruling of May 11, 1995 in this proceeding, the official service list inadvertently failed to include Sprint Communications Company L.P. (Sprint). Sprint and DCA, as well as the others on the service list should be served with the opening and reply comments.

<u>Location</u>	<u>Date</u>
Los Angeles	September 20, 1995, Wednesday
San Bernardino	September 26, 1995, Tuesday
Barstow	September 27, 1995, Wednesday
San Diego	October 2, 1995, Monday
Fresno	October 5, 1995, Thursday
San Jose	October 10, 1995, Tuesday
Sacramento	October 11, 1995, Wednesday
Volcano	October 12, 1995, Thursday
Redding	October 19, 1995, Thursday
Eureka	October 24, 1995, Tuesday

Comments that reply to the opening comments or to issues raised at the FPH, and PPHs, may be filed on or before December 1, 1995. The reply comments shall not exceed 25 pages.

After receipt of the opening comments, the Commission may issue an interim decision regarding where cost studies for the purpose of determining high cost GSA will be addressed, and the format of those studies. Additional interim decisions or rulings may be needed to lay the groundwork for the universal service rules, and to adopt the final rules. At this time, it is envisioned that once the cost studies determine the subsidy needed for the high cost voucher mechanism, a final decision will be issued around June 1996 implementing the universal service rules.

#### Findings of Fact

1. On January 24, 1995, the Commission opened this universal service OIR/OII to develop rules to pursue universal service goals in a competitive telecommunications environment.

2. Comments to the universal service OIR/OII were filed by commenting parties in March 1995.

3. On or about June 23, 1995, DCA filed a motion to accept the late filing of its comments and recommendations to the universal service OIR/OII.

4. AB 3643 states that participation by the State and Consumer Services Agency should be encouraged.

5. Universal service means essentially two things: (1) that a minimum level of telecommunication services are available to virtually everyone in the state; and (2) that the rates for such services remain reasonable.

6. The universal service concept that rates remain reasonable has resulted in the development of the CHCF and the ULTS programs.

7. The CHCF ensures that both residential and business customers in high cost service areas of the small and medium sized LECs have access to telephone services at reasonable prices.

8. The CHCF allows the small and medium size LECs to receive funds to recover the relatively high network costs of providing exchange services in less profitable and high cost areas of the state.

9. Pacific and GTEC do not draw funds from the CHCF because their higher cost areas are internally subsidized by the more profitable exchanges, subsidies between product lines, and other sources of revenues.

10. The statewide ULTS program ensures that low income households have access to basic telephone services at a fixed and affordable price.

11. In D.94-09-065, the Commission recognized that Pacific and GTEC needed to significantly improve their customer outreach and educational programs to achieve a 95% penetration rate for phone service among low income, nonwhite, and non-English speaking households, and ordered Pacific and GTEC to file monitoring plans regarding penetration rates.

12. The 95% goal represents a Commission commitment to ensure that all populations in California are afforded universal service, and that technological advancements benefit all segments of the population.

13. CLCs, and incumbent LECs other than Pacific and GTEC, should be required to submit in their annual reports, their efforts

and achievements to improve telephone penetration rates in their service territories, especially among nonwhite, non-English speaking, and low income households.

14. The Commission can position education, health care, community, and government institutions to benefit from the information age by creating and fostering the development of a competitive market.

15. The fourth stated objective of AB 3643 refers to the development of a process to periodically review and revise the definition of universal service to reflect new technology and markets.

16. AB 3643 states that there must be an ongoing evaluation of which services are deemed essential and therefore a part of universal service.

17. Basic service represents a set of telecommunications capabilities which consumers receive when they order service from a LEC.

18. The basic service definition serves as the basis for deciding how much low income customers should be subsidized under the ULTS program, and what services should be subsidized in high cost areas.

19. DRA, UCAN, and the Coalition's definitions of basic service generally reflect the level of basic service that Californians currently enjoy.

20. Pacific and GTEC's definitions of basic service advocates a minimal nationwide definition which retreats from established Commission policy.

21. In establishing a procedure to reevaluate basic services, the Commission needs to adopt a process for initiating review, and to select criteria for evaluating whether a service should be included in basic service.

22. UCAN and USA have proposed grant or funding programs to help in the development of new products and services.

23. The Commission is concerned about the possible redlining of information poor communities.

24. It appears that the telecommunications market is already moving toward digital access.

25. The Commission is committed to guaranteeing that high quality basic telecommunications services remain available and affordable to all Californians.

26. The mechanism for universal service in a competitive environment must ensure that low income customers have access to affordable service and that high cost areas of the state receive support so that telecommunications services will remain affordable throughout the state.

27. With the introduction of competition into all areas of California, the Commission needs to reexamine both the ULTS and CHCF programs.

28. High cost areas are not restricted solely to areas within the territories of the small and medium size LECs, but include certain service areas of Pacific and GTEC as well.

29. Local exchange competition should be permitted before final universal service rules are adopted.

30. The current universal service funding mechanisms should remain in place during the transition to local exchange competition.

31. Competition will take time to develop.

32. Cost studies are needed to confirm the extent to which the LECs' residential basic exchange services are being subsidized.

33. Based on the comments, the low income and high cost universal service programs should remain separate.

34. PU Code § 709.5(a) states the intent of the Legislature that all telecommunications markets subject to the Commission's jurisdiction should be opened to competition no later than January 1, 1997.

35. PU Code § 709.5(c) provides that the Commission should take the necessary steps to put into place whatever additional rules and regulations that may be necessary to achieve the January 1, 1997 date.

36. The focus of the CHCF is on subsidies for the smaller LECs, rather than a subsidy of the smaller LECs' residential or business customers.

37. The COLR is the regulatory concept that there must always be a provider that is obligated to serve all customers in a particular service area.

38. With the introduction of competition, certain providers may choose to serve a smaller service area than what the incumbent LEC is obligated to serve.

39. The voucher system for high cost areas would work by giving the customer a credit voucher for a set amount of money which represents the difference between the actual cost of serving a customer and a rate that is deemed affordable by the Commission.

40. With a virtual voucher, the carrier selected by the customer would credit the customer's bill with the subsidy amount, and receive payment from the fund.

41. The auction or bidding mechanism allows qualified providers to bid a fixed amount of subsidy necessary to serve a high cost area.

42. Under the auction mechanism, there does not appear to be any incentives for bidders to bid down the subsidy required to serve a particular area.

43. If an auction mechanism is chosen, it is likely that the Commission or its designee would have to become involved in numerous service territory auctions.

44. The high cost voucher fund differs from the CHCF in that all areas of the state with high cost areas can be subsidized, all providers in high cost areas can draw from the fund, and the

smaller LECs' revenue requirement is not tied to the high cost voucher fund.

45. Cost studies are a good starting point for determining whether a subsidy is needed, how large the subsidy should be, and how the subsidy should be targeted.

46. In the design of a funding mechanism for high cost areas of the state, the use of large study areas results in cost averaging of high cost and low cost areas.

47. The GSAs will serve as reference points from which cost data can be derived, and from which the subsidies for the designated COLR or COLRs can be derived.

48. A GSA which is smaller in size lessens the effects of cost averaging between customers, and prevents barriers to entry.

49. Upon the completion of the cost studies relating to high cost areas in the OANAD proceeding, the total subsidy for high cost areas can then be used in this proceeding.

50. In deciding how high cost GSAs should be determined, the Commission needs to establish a reference or benchmark as a point of comparison.

51. When a carrier undertakes the COLR obligation, the Commission needs to ensure that the community in which the COLR is serving will have a carrier who is capable of fulfilling that obligation.

52. The Commission uses an AEUS to fund both the ULTS program and the CHCF program.

53. TURN's proposed funding mechanism for high cost areas is based on the net trans account idea developed by Professor Noam.

54. Any universal service funding plan requires a funding administrator to collect and deposit contributions into the fund, and for disbursing the money to the appropriate carriers.

55. The funding level for ULTS is not expected to increase significantly.

56. The Commission wants to ensure that residential consumers have a sufficient amount of information available to them so that consumers can make informed choices about their telecommunications provider and available services.

57. Residential consumers should have information available to them which allows for an easy comparison of rates.

58. D.89-10-031 sought to disassociate rates from depreciation practices.

59. The excessive amortization period that GTEC and Pacific complain of has been diminishing as the expected life for depreciation purposes has been steadily reduced.

60. Investments made in anticipation of competition should not be regarded as stranded investment.

61. The assets associated with serving high cost areas will not be stranded if the incumbent LEC continues to serve the service area, or if it resells to other providers.

#### Conclusions of Law

1. DCA's motion to accept the late filing of its comments and recommendations should be granted.

2. Providing special rates to certain classes of customers to the exclusion of others for the same type of services may be contrary to PU Code § 453, and its prohibition against discriminatory rates and charges.

3. The reference in AB 3643 to a review process of the definition of universal service was meant to refer to a review process of the definition of basic service, because the reference in AB 3643 to an ongoing evaluation of which services are deemed essential suggests that essential services make up the definition of basic service.

4. Basic service defines a level of basic service which all local exchange providers must adhere to in California.

5. The definition of basic service should include the elements contained in proposed Rule 4.B.

6. The proposed definition of basic service is a reasonable definition of what are essential telecommunications services, and reflects what telephone customers have come to expect.

7. The definition of basic service should be the same for all local exchange providers.

8. The Commission should adopt a periodic, formal review of the definition of basic service as set forth in proposed Rule 4.C.

9. The Commission should adopt the criteria set forth in proposed Rule 4.C.2. as the criteria for reevaluating the definition of basic service.

10. The Commission should not propose a rule at this time to fund the types of programs proposed by UCAN and USA.

11. The universal service mechanisms need to be redesigned to allow new market entrants access to those funds, and to reflect the downward pressures on costs that competition should bring.

12. In accordance with PU Code § 709.5, the redesign of universal service should apply to all service areas within the state.

13. The Commission proposes to replace the current CHCF with the high cost voucher fund, and that an auction mechanism be used as a safety net in the event no single provider is willing to undertake the COLR obligation in any area of California.

14. The high cost voucher fund should subsidize residential customers rather than implicitly subsidizing both business and residential customers through service revenue cross subsidies as is true of current carrier rate designs.

15. A designated COLR should be required to serve areas based on GSAs.

16. The Commission should adopt census block groups as the GSAs.

17. The cost studies should be developed by way of proxies for all the GSAs in accordance with proposed Rule 6.A.