

# PETITION

We the undersigned do hereby request that the FCC approve Southwestern Bell's application to offer long distance service in Oklahoma.

NAME	ADDRESS	TELEPHONE NUMBER
Donna Rodgers	517W Carl Albert	426-6744
Kathleen Saveman	19035 137h.	423-2861
Betty Spann	PO Box 3029	426-1286
Jeff Bealand		297-2347
Paul Ryan		429-0790
Amelia M Jones	811 E Pierce	423-1065
Dustin Lennards	130 Fairview	426-4089
Debra Bell	Rt. 6, Box 318	426-1787
Jammy Patten	1101 W. STONEWELL	423-3610
Louise Rapone	Rt 2 Stuart, Ok	546-2566
Robert Morito	805 Kinkead Rd	423-7139
Jul Moore	1231 Dan St.	465-5204
Eddie Parker	Rt. #6 Box 45.	423-7982
Pauline Ragland	501 W. Kiowa	423-8320
Helen Peters	312 W. Park	426-6631
Kevin Beal	2010 N. 19th	426-6921
Ruby Link	129 Chestnut Hartshorn Ok	297-2749
Ron Seelman	210 W. Ave. Dewar	423-7641
Violet Swaffar	534 W. North	423-0633
Connie Woods	8195 612 Mc	918-423-3430

# PETITION

We the undersigned do hereby request that the FCC approve Southwestern Bell's application to offer long distance service in Oklahoma.

NAME	ADDRESS	TELEPHONE NUMBER
Wm J. Jaramila	6048 Strong Blvd McAlester Ok	423-1268
Sandra Sweeney	802 Beard Mad. U. Ok	795-7506
Jeremie Sue Bridgeman	P.O. Box 219 Selmon, Ok	405-795-2539
Kevin J. Jaramila	3601 View Circle McAlester	423-7845
Aana Holt	Rt 4, Box 225 McAlester,	423-8531
Lyn Roberts	1303 S. 17th McA, 426-0704	
Berry Selman	HC 75 Box 5 HAYWOOD	426-0233
Sammy Skay	300 Rock Rd MC	426-3650
Kathy Mason	Rt. 5 Box 450 McA	423-0549
Mark J. Jaramila	501 E. Oage	423-9419
Mary J. Speed		423-8960
J. R. Hudnicki		423-5580
Mary Liddle		423-5949
LaShonda Hutchings	Box 115 McAlester	423-6381
Joyce Davis	Rt. 2 Box 127 Nowen	532-5382
Angie Lee	Rt. 2 Box 164 Tecumseh	598-5453
Nobbe Brock	Rt 4, Box 428, McAlester, Ok 74501	918-423-5432
Laura McCullar	Box 195 Haileyville Jk	74546
Dr. J. J. Jaramila	McAlester Ok.	
Cleo Hancock	1020 Kirkwood Rd McAlester, Ok	74501

# PETITION

We the undersigned do hereby request that the FCC approve Southwestern Bell's application to offer long distance service in Oklahoma.

NAME	ADDRESS	TELEPHONE NUMBER
S Mackey	PO Box 343 Krebs	426-4286
Cynthia Hapold	HC 62 Box 74E Eufaula	689-4700
Melanie Roberts	P.O. Box 1961 McAlester	918-389-4686
James W. Smith	Rt 6 Box 34 McAlester	918-423-2328
Bruce Almy	P.O. Box 479	297-0005
Pat Lake	5201 W. Chamberl	423-4917
Helena Henards	1411 South Ave McA	423-1630
Odis Trammell	Rt 1 Box 554	423-6824
Eugene L. [unclear]	4620 S Parkhurst McAlester	426-6286
Jim Lewis	301 E Beck McAlester	426-3153
Janice Crews	1900 Hereford Cir. McAlester	423-1121
Reba Akode	2207 Sycamore, McAlester	429-044
Jan STROBE	2207 Sycamore, McAlester	429-044 1
Maxine Ball	1019 Rosebrier Dr Guthrie	-405-282-1218
Judy Douglas	Rt 8, Box 604, McAlester	
Denise Weaver	Box 72 Alderson	
Patchery [unclear]	PO Box 636 Krebs	423-7739
Jim Mullins	37 W Apache	426-1737
Daphne Hollingsworth	1102 Hwy 270 E	
Wanda Midgett	905 E. Delaware, McAlester	423-5449



CC 76-45

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# Public Service Commission of Wisconsin

Cheryl L. Parrino, Chairman  
Daniel J. Eastman, Commissioner  
Joseph P. Mettner, Commissioner

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610 North Whitney Way  
P.O. Box 7854  
Madison, WI 53707-7854

April 28, 1997

Chairman Reed Hundt  
Commissioner James Quello  
Commissioner Susan Ness  
Commissioner Rachelle Chong  
Federal Communications Commission  
1919 M Street NW  
Washington DC 20554

BY RECEIVED

JUN 10 1997

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

Re: In the Matter of Federal-State Joint Board on Universal Service

Dear Commissioner Ness:

Next week you will be making one of the most important decisions on telecommunications since divestiture. Structuring a universal service plan to assure reasonably available and affordable services to all is a challenge, and your determinations will be critical to the entire nation.

The universal service decision will address many issues, on most of which there are divergent points of view. All the issues are complex or controversial. I would like to share some brief observations and opinions on a few of these items.

### *Proxy Models*

I understand the goal of proxy models as used in the universal service context is to simplify the process of determining costs. Based on experience, I recognize that cost studies are expensive and can be time intensive from a regulatory perspective. I would like to see a process that minimizes costs and regulatory intervention; however, I agree with Joint Board Commissioner Julia Johnson that none of the proxies in this proceeding is ready for use. On this matter, I urge you not to make a final decision. As this whole cost issue is examined in the months ahead, I would encourage the FCC (and the continuing Joint Board) to consider more reliance on state commission efforts to identify the costs of service.

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### *Transition Plan*

I support the position of the state members of the Joint Board that encourages use of the alternative transition plan as part of the overall universal service decision. The initial Joint Board decision presents a grave potential to harm rural areas and actually diminish universal service. The alternative plan maintains more support for rural areas and companies. It offers continued incentives for infrastructure investment, avoids an immediate potential for local rate increases, and supports expanded service and growth in the rural areas.

The various provisions of the transition plan, including continued universal service support for second residential lines and business lines, will protect universal service in all parts of the nation.

Chairman Reed Hundt and Commissioners  
Federal Communications Commission  
Page 2

***The Universal Service Challenge***

I am very aware of the challenge this case presents. As a commissioner for several years, I have been in your shoes as you attempt to minimize costs while maintaining support for the many goals encompassed in the concept of universal service. I believe attention to meeting these goals is of paramount importance. Meeting all these needs may require a measured and reasoned approach that recognizes all goals may not be achievable at once. The impacts of these universal service provisions on local rates could be so high as to negate the very intentions of the universal service fund programs. It would be the ultimate irony if steps taken to protect and promote universal service were in fact a contributor to its downfall.

***Joint Boards***

The Joint Board process is not painless, but it works. I support continued reliance on this process to shepherd further universal service changes. I applaud the public comments by Chairman Hundt on a commitment to ongoing Joint Board involvement. The work of the separations Joint Board—in process now—will be a critical input in the ongoing evaluation of universal service.

***Access Charges***

Some access charge reductions are needed; however, careful weighing of goals is required. Overzealous access charge reductions could jeopardize support for rural areas and low income customers and increase pressures for increases in local rates.

In conclusion, I support your efforts and recognize your challenge. I encourage you to consider these comments as you deliberate these important issues.

Sincerely,



Cheryl L. Parrino  
Chairman

CLP:GAE:jah:h:\ss\letter\FCCJoint BdUSF-4-28-97-GAE

cc: Brad. Ramsay, NARUC  
John F O'Neal, NRTA  
Michael E. Brunner, NTCA  
John N. Rose, OPASTCO  
Roy M. Neel, USTA  
Governor Tommy G. Thompson

BOBBY L. RUSH  
1ST DISTRICT  
ILLINOIS

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CONGRESS OF THE UNITED STATES  
HOUSE OF REPRESENTATIVES  
WASHINGTON, D.C. 20515

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

April 30, 1997

→ KBL

JSB

The Honorable Reed E. Hundt, Chairman  
Federal Communications Commission  
1919 M Street, N.W. Room 814  
Washington, D.C. 20554

Dear Chairman Hundt:

We are writing you to express the strong support of the Congressional Black Caucus (CBC) for universal service funding to connect schools and libraries to the information highway. Access to computers is a high priority to the CBC agenda.

The children of our nation are our most precious resource, and their educational development is critical to our national security. Unfortunately, children in rural areas and in under-resourced communities are on the verge of being shut out from access to the information highway, the gateway to their development.

Studies show that by the year 2000, 60 percent of all jobs will require the ability to use a computer. While 62 percent of schools serving students from relatively higher income families provided access to the Internet at school, only 31 percent of schools serving a large proportion of students from poor families provided similar access. Eight-two percent (82%) of high school students from the most affluent families had access to computers at home, while only 14 percent of poorer high school students had computers at home.

The Federal Communications Commission (FCC) must take affirmative steps to ensure that small schools, rural schools, schools in the poorest areas of our country, and schools with large minority populations have access to the information highway and technology based learning. This is critical since the Thomas Rivera Center in its study of Latinos and Information Technology found that schools are the primary gateway to technology for Hispanic and African American children.

When Congress passed the Telecommunications Act of 1996, it recognized this critical problem and mandated a universal service policy. The Act requires the FCC to provide discounts to schools, libraries, and rural health centers for access to telecommunications services. On November 7, 1996, the Federal-State Joint Board on Universal Service, established by the Act, made recommendations to implement universal service, including:

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The Honorable Reed E. Hundt, Chairman  
April 30, 1997  
Page 2

1) establishing a discounted rate from 20-90 percent, to connect schools and libraries to telecommunications services. Eligible services would include Internet access, internal connections, installation and maintenance;

2) creating a Universal Service fund of \$2.25 billion a year to connect schools and libraries. The funding would be derived from fees paid by telecommunication service providers;

By May 8, 1997, these recommendations will be voted on by the FCC for final approval.

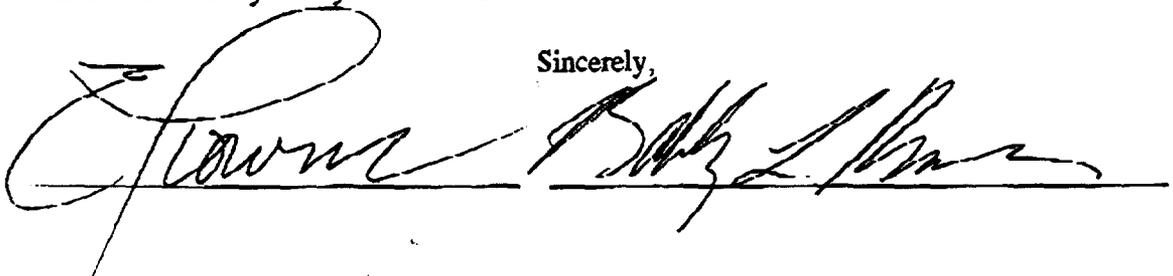
The Congressional Black Caucus strongly endorses the Universal Service Federal-State Joint Board recommendations for connecting our classrooms and libraries. Funding to link our schools and libraries to the Internet must be implemented immediately. Given the existing access gaps, our children and communities cannot afford a moment's delay in getting on the information highway.

As we approach the end of this century, we are at a pivotal time in the development of our Nation. The challenges that we face as a Nation in ensuring that every child has access to advanced telecommunications in school are as profound as the challenges we faced early in this century when our Nation set about the task of ensuring free public education to every school-aged child in America. This challenge is a legacy of the battle we fought in the middle of this century to integrate the public schools. Like those pivotal times, we can choose a policy of opportunity and hope for all of our Nation's children, or we can perpetuate divisions.

We have a common goal: to ensure that children in rural and under-resourced areas of our country have every tool and every opportunity to learn and to contribute to America's future. We are proud to support universal service connection for our classrooms, schools, and libraries.

We will be happy to discuss this vital issue of importance to our children and to our communities with you at your convenience.

Sincerely,

A large, stylized handwritten signature in black ink, likely belonging to Reed E. Hundt, is written over a horizontal line. The signature is cursive and somewhat abstract, with a large loop at the beginning.

The Honorable Reed F. Hundt, Chairman

April 30, 1997

Page 3

Bill Gellman Hubert Seal

James Millender James George H. North

Robert H. Hastings Melvin P. Watts

Wm M. Clayton Scott D. Ho

Albert R. Lyman Wayne R. Jones

Donald W. Layne Maline Watson

Tom A. Long Ed E. Cummings

James E. Clifton R. M. C. Arnold

Danny L. Davis William L. Clay

J. A. O'Neil Julia C. ...

The Honorable Reed E. Hundt, Chairman

April 30, 1997

Page 4

<i>Robert V. Bell</i>	<i>Chick Fattah</i>
<i>Earl F. Hilliard</i>	<i>Eddie Bernice Johnson</i>
<i>Tommy J. Pappas</i>	<i>Shirley Jackson Lee</i>
<i>John Lewis</i>	<i>Carolyn C. Fitzpatrick</i>
<i>John Dingens</i>	<i>Samuel Alito</i>

**Copies to:**

**Commissioner James H. Quello**  
**Federal Communications Commission**  
**1919 M. Street, N.W. Room 802**  
**Washington, D.C. 20554**

**Commissioner Rachelle B. Chong**  
**Federal Communications Commission**  
**1919 M Street, N.W. Room 844**  
**Washington, D.C. 20554**

**Commissioner Susan Ness**  
**Federal Communications Commission**  
**1919 M Street, N.W. Room 832**  
**Washington, D.C. 20554**

**Senator John McCain, Chairman**  
**Committee on Commerce, Science, and Transportation**

**Senator Conrad Burns, Chairman**  
**Subcommittee on Transportation**

**Representative Thomas J. Bliley, Chairman**  
**Committee on Commerce**

**Representative W.J. Tauzin, Chairman**  
**Subcommittee on Telecommunications, Trade, and Consumer Protection**

**Federal Communications Commission Federal-State Joint Board Members**

**Secretary Richard Riley, U.S. Department of Education**

CC:96-45

970207

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STATE OF CALIFORNIA — STATE AND CONSUMER SERVICES AGENCY

PETE WILSON, Governor



LEGAL AFFAIRS

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SACRAMENTO, CA 95814-6200

Telephone: (916) 445-5126  
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April 9, 1997

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

→ 726-172

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[Redacted]

Chairman  
Federal Communications Commission  
1919 M Street, N.W., Room 814  
Washington, D.C. 20554

The Honorable Rachele B. Chong  
Commissioner  
Federal Communications Commission  
1919 M Street, N.W., Room 844  
Washington, D.C. 20554

The Honorable Susan Ness  
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Federal Communications Commission  
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The Honorable Kenneth McClure  
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Missouri Public Service Commission  
301 W. High Street, Suite 530  
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The Honorable Julia Johnson  
Commissioner  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
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The Honorable Sharon L. Nelson  
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Washington Utilities and  
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The Honorable Laska Schoenfelder  
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Regina M. Keeney, Chief  
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Federal Communications Commission  
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Gentlepersons:

The California Department of Consumer Affairs ("DCA") commends you for your effort to implement the federal Telecommunications Act of 1996 ("TCA") in ways that are economically sound, forward-looking, and public-spirited. As the Information Age unfolds, your resolution of the issues raised by the TCA and the new technologies will become increasingly important to everyone.

The purpose of this letter and the enclosed white paper is to emphasize DCA's concern about the Joint Board's recommendation that the Commission fund a federal high-cost area subsidy through a charge on the net income of providers (a "net trans account") instead of an all end user surcharge ("AEUS").

Reed E. Hundt  
April 9, 1997  
Page 2

The DCA, which represents consumers of all income levels, is participating in proceedings of the California Public Utilities Commission ("CPUC") to open the local exchange market to competition, and is keenly interested in exploring how to best achieve the goals of universal service and fund any needed subsidies. From both individual consumer and societal standpoints, DCA believes that the explicit, disclosed, customer surcharge is the preferred option for any universal service subsidy program. The lack of definition of what constitutes universal service, the potential size of the subsidy, its potential for deterring innovation, the potential for hurting consumers who are sought to be helped, the phenomenally rapid changes in the market, the complexity of the technical, economic and legal issues, and the concept of openness of government, combine to decide the issue.

If a net trans account were used, the effect would be to hide the funding from the public. Making coerced subsidies explicit helps achieve a subsidy process that is efficient and democratic. An AEUS promotes openness and candor in regulation and the market. It identifies the amount of the subsidy, which customers pay it, and which customers receive it. It helps to "keep things in the open" and provide the best opportunity for correction where needed. Universal service subsidies, by their very nature, disadvantage some groups of customers or services in order to benefit other groups of customers or services. All groups have an interest in knowing in what respects they are benefitted or burdened, so that they can voice their concerns if they disagree with the decisions that the government is making on their behalf. The AEUS is also competitively neutral. It assures that the subsidy contribution is uniform across carriers and across services. Retail customers cannot affect their contribution by changing carriers or the mix of services purchased. Thus, an AEUS minimizes the effect of the contribution on the customer's purchase decision. Like a sales tax, an AEUS provides reasonable assurance that the burden of a government-mandated subsidy program is borne by and known to all customers -- residential and business, large and small.

There is special reason to provide a mechanism of this kind for funding universal service subsidies. The telecommunications process and its cost accounting are complicated and not thoroughly understood even by experts. The potential dollar volume of the universal service subsidy is enormous. A poorly-crafted subsidy process will impair the efficiency of the telecommunications process by imposing costs for which there are no commensurate benefits. The interests of, and equities among, different classes of customers are difficult to define. The concept of universal service (even in a static market) is ill-defined. The goals of universal service are changing as technology evolves. Each of these factors invites the most careful policymaking, auditing, feedback, and improvement processes. Their combined presence makes the presence of a workable auditing, feedback, and improvement process essential.

Economic factors also point to an AEUS as the preferred option. As viewed by Bruce Egan in Information Superhighways Revisited: The Economics of Multimedia, "[d]irect subsidies, especially of the current untargeted variety, are ... not socially efficient. The current flow of toll-to-local, urban-to-rural and large telco to smaller telco subsidies, is generally inefficient because it is not based on need ...."<sup>1</sup> Egan notes that "the advent of competition in local telecommunications markets makes it imperative to conduct a more formal economic analysis to measure the social costs and benefits of universal service policies ...." He argues that "universal service funding mechanisms need to be

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<sup>1</sup> Egan, Bruce L., Information Superhighways Revisited: The Economics of Multimedia (Boston: Artech House, 1996), p. 307.

Reed E. Hundt  
April 9, 1997  
Page 3

designed and implemented in a manner that is viable in a competitive environment and that provides the least distortion of the benefits of competitive markets."<sup>2</sup>

Overcharging one customer group or service in order to benefit another customer group or service distorts market signals and thereby misdirects research, product development and marketing, resulting in inefficient markets, in the unavailability of services that might otherwise be provided, and, overall, in the industry's provision of relatively less value to all customers and to society. In an industry where continuing advancements are important to both the economy and individual customers of all income levels, a surcharge is essentially a tax on an important and presumably favored activity. Like all taxes, it deters rather than spurs that activity. Although some level of subsidy to support universal service goals will promote the overall efficiency of the public network, a subsidy that is excessive will be counterproductive. An AEUS will help assure that the subsidy does not become excessive.

Since the percentage of the average consumer's monthly bill that is attributable to local voice telephone service is declining, it is important that universal service issues be addressed with competence and precision, so as not to deter deployment of advanced services that consumers may desire, use and be willing to pay for. If the public switched telephone network is to evolve in ways that will accommodate "distant learning" and other broadband applications, and not force consumers to rely on alternative and probably more expensive telecommunications systems to work at home, takes courses, etc., it is necessary to upgrade the public network to permit those applications, and not burden its evolution by programs of cross-subsidy that deter rather than promote development.

Some people believe that an AEUS is not a politically palatable funding mechanism -- that it is better not to inform consumers about what is being done for consumers. That is ironic. If the present system of regulation-mandated cross subsidies is unsound, and if this results from fear that consumers will be irrational in evaluating the behavior of legislators and regulators,<sup>3</sup> the best antidote is to educate consumers, not keep them in the dark. The AEUS will help educate consumers (both those who fund and those who receive subsidies) by making the practical impacts on them explicit.

Now may be the only time that a competently-designed funding process can be put in place. Once the state and federal universal service systems are implemented, it will be as difficult to modify them as it is to modify other major social programs. At this point in the evolution of telecommunications, the U.S. is fashioning a process that could prove to be as large and inappropriate (and perhaps also counterproductive) as the tax subsidy to housing (a \$85 billion program that mainly benefits the most affluent), support to agriculture that goes mainly to large farming organizations, or a deposit insurance program that invites large taxpayer bailouts.

The enclosure discusses the economic, policy, and legal implications of the two methods of financing universal service. It also provides a legal basis for concluding that Section 254(d) of the TCA does not preclude the use of an AEUS, and addresses other arguments made against an AEUS.

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<sup>2</sup> Id., at pp. 228, 231.

<sup>3</sup> This is the view advanced in Kaserman, David L. and John W. Mayo, "Cross-Subsidies in Telecommunications: Roadblocks on the Road to More Intelligent Telephone Pricing," 11 *Yale Journal on Regulation* (Winter 1994), 119 at 142-146.

Reed E. Hundt  
April 9, 1997  
Page 4

We hope that this letter and the enclosed paper will provide a basis on which the Commission can adopt an AEUS funding mechanism for federal universal service programs, as the CPUC has done in California.

Thank you for your attention and consideration.

Sincerely,



VIRGINIA J. TAYLOR  
Staff Counsel



RICHARD A. ELBRECHT  
Supervising Attorney

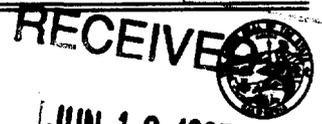
Enclosure

cc: Peter Arth, Jr.  
Lionel B. Wilson  
Mary Mack Adu  
Gretchen Dumas

(g:\ls\vjt\telecomm\letters\fcc4.8B)



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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

## **Financing Universal Service: All End User Surcharge Versus Net Trans Account**

March 10, 1997

The concept of "universal telephone service" dates back to the early 1900s. However, the meaning of that concept has changed significantly since its inception, when it referred to interconnection, and not social or geographic ubiquity.<sup>1</sup>

Most recently, universal service has come to mean, generally, that every citizen should be able to obtain some form of minimum basic telephone services at reasonable rates. As expressed by the California Public Utilities Commission ("CPUC") in a 1992 report on universal service:

The public policy basis for the Universal Service goal is both that the value of the network increases as more customers are connected, and that the telephone is a basic tool needed for integration into today's society and is necessary to help provide a decent standard of living in our nation.<sup>2</sup>

Over the past 20 years, various state and federal programs have been implemented to help assure the universal availability of telephone service at a reasonable price.<sup>3</sup> Those programs have been funded through various means, among them a tax on the revenues of telecommunications carriers, and a user surcharge on the amounts billed to telecommunications customers.

The recent opening of the local exchange telecommunications market to competition in California, and the passage of the federal Telecommunications Act of 1996, have raised the need to redesign mechanisms to fund the universal service programs in a competitive marketplace.

The issue also has been raised by the recent filing of a complaint in federal court by The Utility Reform Network ("TURN", formerly "Toward Utility Rate Normalization"), a

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<sup>1</sup> Mueller, Milton, "Universal service in telephone history," Telecommunications Policy (July 1993), 352, 364.

<sup>2</sup> "Universal Service Issues in the Telecommunications Industry: Final Report on June 29, 1992 Workshop", Commission Advisory and Compliance Division, California Public Utilities Commission, October 16, 1992, at p. 1

<sup>3</sup> See, California Public Utilities Code section 871.5(a).

consumer activist group, against the CPUC. TURN's Complaint alleges that the funding mechanism adopted by the CPUC -- an all end user surcharge ("AEUS") -- violates federal law.

All of these events underscore the need to identify and analyze the economic, policy, and legal bases for those two methods of funding universal service programs -- a tax on the revenues of carriers, and a user surcharge on amounts billed to customers.

This paper:

- examines how universal service programs have been funded in past years in California;
- reviews the policy basis for adopting an AEUS, instead of a surcharge on the net revenues of telecommunications carriers ("a net trans account"), as the most desirable funding mechanism for universal service programs in an open and competitive marketplace with numerous providers; and,
- analyzes arguments made by opponents of an AEUS, such as the assertions made in the action by TURN against the CPUC.

## I. BACKGROUND OF COMPETITION IN THE TELECOMMUNICATIONS INDUSTRY.

The U.S. telecommunications industry was once the principal domain of a single monopoly telecommunications carrier -- AT&T. That circumstance was dramatically changed in 1984 with the court-approved divestiture from AT&T of its local operating companies, a divestiture to which AT&T and the U.S. Department of Justice had agreed in a settlement of the government's antitrust action against AT&T.<sup>4</sup> While competition began to develop in the interstate and interLATA (local access and transport area) telecommunications marketplaces, the intraLATA markets remained largely in control of the seven Regional Bell Operating Companies ("RBOCs"), which continued to enjoy the status and protection of legal monopolies.

In the late 1980s and early 1990s, as the potential for open competition in other areas of the telecommunications market increased, the continuation of the legal monopoly status and associated regulation of the incumbent local exchange carriers ("ILECs") came under scrutiny. Numerous proceedings in California and other states were instituted to eliminate the legal monopoly status of ILECs and open the local markets to entry by competitors. In California, the CPUC opened the intrastate intraLATA toll market to competition beginning

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<sup>4</sup> Competitive Impact Statement in Connection With Proposed Modification of Final Judgment, 47 Federal Register 7170 (February 19, 1982).

January 1, 1995,<sup>5</sup> and, the year, the CPUC also commenced proceedings to open the local exchange markets to competition.<sup>6</sup>

As part of that process, and as required by California Public Utilities Code section 871.5(d), the CPUC recognized that subsidized services to some groups of customers, particularly those which had been funded through internal cross-subsidies of the large ILECs, would have to be funded in some other way in order to function in a competitive market environment in ways that would be equitable, broad-based, and competitively neutral.<sup>7</sup> Accordingly, the CPUC opened a proceeding to determine how those universal service programs should be provided and funded.<sup>8</sup>

## **II. BACKGROUND OF CALIFORNIA'S USE OF AN AEUS TO FUND UNIVERSAL SERVICE PROGRAMS.**

The most well-known legislatively mandated universal service telephone program for low-income telecommunications customers in California -- now referred to as "Universal Lifeline Telephone Service" ("ULTS"), or "Lifeline" -- was implemented pursuant to Statutes 1983, Chapter 1143.<sup>9</sup> The Lifeline program funding mechanism established by that legislation was a tax on long-distance telephone companies not to exceed 4% of each company's gross intrastate revenues, with the CPUC given authority to levy the same tax on local telephone companies and other local telecommunications carriers. The tax was payable quarterly to the California State Board of Equalization.<sup>10</sup>

By legislation adopted in 1987, the program, which had been scheduled to expire on July 1, 1988, was continued in effect, but was significantly revised. Among the numerous changes, the tax imposed on every carrier was repealed and, in its place, a rate surcharge

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<sup>5</sup> Re Alternative Regulatory Frameworks for Local Exchange Carriers, California Public Utilities D.94-09-065, filed September 15, 1994, 56 CPUC 2d 117; see also, California Public Utilities Code section 709.2.

<sup>6</sup> Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service, R.95-04-043; and, Order Instituting Investigation on the Commission's Own Motion into Competition for Local Exchange Service, I.95-04-044, ("Local Competition Proceeding") filed April 26, 1995.

<sup>7</sup> AB 3643 (Polanco), Statutes 1994, chapter 278, Section 2(a)(1), (2), (3), and (b)(3); see also, California Public Utilities Code section 871.5(d).

<sup>8</sup> Rulemaking on the Commission's Own Motion into Universal Service and to Comply with the Mandates of Assembly Bill 3643, R.95-01-020; and Investigation on the Commission's Own Motion into Universal Service and to Comply with the Mandates of Assembly Bill 3643, I.95-01-021, ("Universal Service Proceeding") filed January 24, 1995.

<sup>9</sup> California Public Utilities Code section 739.2, and California Revenue and Taxation Code sections 4400-44190.

<sup>10</sup> California Revenue and Taxation Code section 44000 et seq.

was adopted.<sup>11</sup> The 1987 legislation required the CPUC to establish rates, funding requirements, and the funding mechanism for the program.<sup>12</sup> It also specifically required, and continues to require, the CPUC to compel ULTS providers to "apply the funding requirement in the form of a surcharge to service rates which may be separately identified on the bills of customers using those services."<sup>13</sup>

As required by the 1987 legislation, the CPUC adopted an AEUS funding mechanism, whereby each customer's monthly telecommunications services bill (with the exception of Lifeline customers) reflects a surcharge collected by the carrier which is an established percentage of the amount paid by the customer for intrastate telecommunications services.<sup>14</sup>

Acting pursuant to the 1987 legislation,<sup>15</sup> the Commission also decided that the ULTS program should be administered on an industry-wide basis through a trust, with an administrative committee established "to implement the Trust and to be responsible for the receipt and investment of ULTS surcharge monies and for the payment of monies expended by LECs and IECs for actual ULTS costs incurred . . . ."<sup>16</sup> Carriers remit the ULTS surcharge they collect from their customers to the administrator of the Lifeline program.

The 1987 legislation required the CPUC to issue an initial order setting ULTS customer surcharges not exceeding 4.0 percent of the "service rates for telephone service provided by telephone corporations operations between service areas."<sup>17</sup> The 1987 legislation also established a process for subsequent years in which the CPUC annually issues an order for each telephone corporation, setting rates for universal telephone service and establishing funding methods based on the telephone corporation's proposed rates, revenue needs, and funding methods for that year.<sup>18</sup> For instance, a Pacific Bell filing dated April 15, 1994, projected fiscal-year 1994-1995 revenue needs of \$301,597,882 on toll revenue subject to the surcharge of \$5,225,606,000, for a surcharge of 5.77 percent, which was slightly less than its then authorized surcharge of 6.0 percent.<sup>19</sup>

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<sup>11</sup> Statutes 1987, chapter 163, effective July 16, 1987.

<sup>12</sup> California Public Utilities Code section 879(b).

<sup>13</sup> California Public Utilities Code section 879(c).

<sup>14</sup> D.87-10-088 dated October 28, 1987; see, The Moore Universal Telephone Service Act (1987) 25 CPUC 2d 556.

<sup>15</sup> California Public Utilities Code section 879(b).

<sup>16</sup> 25 CPUC 2d at p. 560, see also, at p. 567-68, Ordering Paragraphs 10 and 11.

<sup>17</sup> California Public Utilities Code section 879.5.

<sup>18</sup> California Public Utilities Code section 879(a), and (b).

<sup>19</sup> Filing of Pacific Bell in Compliance with D.87-10-088, dated April 15, 1994.

Following the path set by the CPUC's initial (1987) order made pursuant to California Public Utilities Code section 879.5, ULTS services have since been funded "by a surcharge on all intrastate toll calls, whether carried by a local exchange carrier or an interexchange (long-distance) carrier."<sup>20</sup>

In another bill adopted in 1987, the Legislature provided additional guidance, stating that:

(d) The furnishing of lifeline telephone service is in the public interest and should be supported fairly and equitably by every telephone corporation, and the commission, in administering the lifeline telephone service program, should implement the program in a way that is equitable, nondiscriminatory, and without competitive consequences for the telecommunications industry in California.<sup>21</sup>

The use of an AEUS as a funding mechanism for universal service programs had already been well-established in another universal service program when it was adopted for use in the ULTS program. In 1982, the Legislature enacted legislation creating a program to provide special telephone equipment and services for deaf and disabled customers; that program became known as the Deaf and Disabled Trust Program ("DDTP"). The legislation authorized the CPUC to "establish a rate recovery mechanism to allow telephone corporations to recover costs as they are incurred under this section."<sup>22</sup> In 1984, the Legislature amended that legislation and provided that henceforth the program would be funded through an AEUS of not more than "10 cents ((\$0.10) per month for each telephone line of every subscriber," to be identified as "communications devices fund for deaf and disabled," whose proceeds would be administered as "a separate fund and . . . separate accounting . . . ."<sup>23</sup> In 1988, the statute was modified to require the CPUC to "establish a rate recovery mechanism through a surcharge not to exceed one-half of 1 percent uniformly

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<sup>20</sup> California Public Utilities Commission, Final Report on June 29, 1992 Workshop on Universal Service Issues, October 16, 1992, at p. 9.

<sup>21</sup> Statutes 1987, chapter 849; see, California Public Utilities Code section 871.5(d). Note that even though California Public Utilities Code section 879(c) requires the use of an AEUS funding mechanism, Section 871.5(d) makes reference to the need for the Lifeline telephone service program to be "supported fairly and equitably by every telephone corporation." (Emphasis added.) Thus, it is not uncommon for statutes to make reference to "support" coming from those who directly pay money to the fund administrator -- carriers -- while requiring that the support ultimately be funded through a surcharge on customers' bills. The significance of this fact will be discussed later in this paper.

<sup>22</sup> Statutes 1982, chapter 454, section 148, p. 1880.

<sup>23</sup> California Public Utilities Code section 2881(d); Statutes 1984, chapter 1715, modifying California Public Utilities Code section 2881(d).

applied to a subscriber's intrastate telephone service, both within a service area and between service areas . . . ."24 Therefore, since 1984, state law has specifically required that the DDTP be funded through an AEUS.

A universal service program to subsidize service to customers of rural and small ILECs also has been financed through an AEUS. In 1987, the Legislature adopted legislation requiring the CPUC to develop and implement a program to subsidize the rates of customers of small and rural ILECs.<sup>25</sup> The basis for that subsidy program was the belief that customers of small metropolitan and rural ILECs live in areas where the costs to provide service are higher than customers can afford to pay.<sup>26</sup> Although the legislation did not prescribe the method the CPUC should use to fund that subsidy program, the CPUC elected to use an AEUS funding mechanism. This surcharge appeared on the bill of all California telecommunications customers as a line item identified as the California High Cost Fund.<sup>27</sup>

Pursuant to a Decision 96-10-066 in the Universal Service Proceeding, adopted on October 25, 1996, ("the Decision") the CPUC established two new universal service programs -- the California High Cost Fund-B ("CHCF-B") which subsidizes the rates of customers of California's large and mid-sized ILECs who live in high-cost areas, and the California Teleconnect Fund ("CTF") which subsidizes the rates for schools, libraries, government owned and operated hospitals and health clinics, and community-based organizations. Following the path set by the legislation that had established the use of an AEUS for the Lifeline and the Deaf and Disabled Assistance Programs, as well as the CPUC's decision to use an AEUS to fund the California High Cost Area program, the CPUC decided that both of the new universal service programs should be funded through an AEUS.<sup>28</sup> Pursuant to the Decision, as of February 1, 1997, the California High Cost Area Fund line item which appears on customers' bills will include surcharges for both the CHCF-A and the CHCF-B,<sup>29</sup> and the CTF surcharge will appear as a separate line item on customers' bills.<sup>30</sup>

Not everyone was satisfied with that result. On December 4, 1996, TURN filed with the CPUC an Application for Rehearing of Decision 96-10-066 And Request for Partial Stay ("TURN's Application"). TURN asserted that in the Decision the CPUC erred in two

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<sup>24</sup> Statutes 1988, chapter 242, section 1, modifying California Public Utilities Code section 2881(d).

<sup>25</sup> Statutes 1987, chapter 755, section 2; California Public Utilities Code section 739.3.

<sup>26</sup> Statutes 1987, chapter 755, section 1.

<sup>27</sup> In D.96-10-066, the CPUC redesignated it as the California High Cost Area-A fund ("CHCF-A"). (D.96-10-066, Appendix B, Rule 1.B. and C.)

<sup>28</sup> D.96-10-066, Appendix B, Rules 6.F., and 8.G., respectively.

<sup>29</sup> D.96-10-066, at p. 191-192.

<sup>30</sup> D.96-10-066, at pp. 87-88.

respects: (1) by adopting an AEUS as the funding mechanism for the CHCF-B and the CTF -- the two new universal service programs instituted by the Decision; and, (2) by finding that the local loop is not a shared cost. TURN requested that the CPUC stay implementation of the AEUS for the CHCF-B and the CTF until the CPUC completes a rehearing on that issue.

On January 23, 1997, the CPUC issued a decision denying TURN's request for a stay. As of this date, the CPUC has not taken action with respect to TURN's request for a rehearing on those issues.

### **III. ECONOMIC AND POLICY ANALYSIS.**

#### **A. Overview of Concerns.**

The main consumer rationale for using an AEUS funding mechanism for universal service programs is one of openness in government. When a government agency imposes an identifiable economic burden on consumers that consumers would not otherwise bear in the absence of government action, consumers have a legitimate interest in knowing about the nature and purpose of the assessment, including how much they are paying to and receiving from others, just as (for example) employees have a right to know how much government is withholding from their earnings for tax purposes.

Making coerced subsidies explicit helps achieve a subsidy process that is efficient and democratic. In that way, the subsidy payor and the subsidy receiver are both made aware of the fact and amount of the subsidy. Both payors and receivers know at least roughly what is happening, and can register their approval or concerns to the regulators and their elected representatives. In that way, the democratic process can help sort out the equities on a long-term basis, and can also ensure that the assessment and benefits program is well-designed and legitimate. Consumers have a right to know what they are paying to support universal service, and it is equally important that consumers know when they are the beneficiaries of support that is provided by others.

There is special reason to provide a mechanism of this kind in the funding of universal service because: (1) the telecommunications process and its cost accounting are complicated and not well understood even by experts; (2) the potential dollar volume of the universal service subsidy is enormous; (3) a poorly-crafted subsidy process will impair the efficiency of the telecommunications process by imposing costs on society for which there are no commensurate benefits; (4) the equities among, and interests of, different classes of customers are difficult to define; (5) the concept of universal service (even in a static market) is ill-defined; and, (6) what constitutes universal service is rapidly changing as technology evolves. Each of these factors alone would invite the most careful policymaking, auditing, feedback, and improvement processes. The combined presence of all of them makes the presence of a workable auditing, feedback, and improvement process essential.

The advantages of the AEUS system are significant. California already has several AEUSs in place. It is easy to administer. Most importantly, it identifies the amount of the subsidy, which customers pay it, and which customers receive it, and it thereby promotes

openness and candor in regulation and the market. Universal service subsidies disadvantage some groups of customers in order to benefit other groups of customers. Both groups have a natural interest in knowing in what respects they are benefitted or burdened, so that they can voice their concerns if they disagree with the decisions that the government is making on their behalf.

In his recent book, Information Superhighways Revisited: The Economics of Multimedia,<sup>31</sup> Bruce Egan points out that "the advent of competition in local telecommunications markets makes it imperative to conduct a more formal economic analysis to measure the social costs and benefits of universal service policies ...." He argues that "universal service funding mechanisms need to be designed and implemented in a manner that is viable in a competitive environment and that provides the least distortion of the benefits of competitive markets."<sup>32</sup> In this subject area and at this time, the potential for an unprincipled universal service program that is injurious to both consumers and the entire economy is enormous.

In assessing the merits and shortcomings of the two methods of funding universal service programs, account must also be taken of the possible disadvantages of the "net trans account." These were identified by the CPUC in its decision adopting the AEUS funding method -- requires new tracking systems, has potential for gaming among carriers, might affect carrier's choice of transmission technologies, and problems in deciding what kinds of technology carriers should be subject to the charge<sup>33</sup> -- seem to far outweigh any real benefits of the net trans account.

In contrast, an AEUS assures that the subsidy contribution is uniform across carriers, and across services. Retail customers could not affect their contribution by changing carriers, or by changing the mix of services purchased. Thus, an AEUS minimizes the effect of the contribution on the customer's purchase decision, and is competitively neutral.

An AEUS is the most appropriate mechanism for funding universal service programs because it is unquestionably explicit and competitively neutral. Those elements are important principles to be followed in establishing any subsidy mechanism. The AEUS becomes an even more important element of the universal service subsidy program funding because it is only through the AEUS that consumers would be aware of the existence of the subsidy program and its cost.

Some people believe that an AEUS is not a politically palatable funding mechanism -- that it is better not to inform consumers about such matters. Yet, the DCA believes that there is no question that the AEUS is most fair and just to consumers. Consumers have a

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<sup>31</sup> Boston: Artech House, 1996.

<sup>32</sup> Egan, Bruce L., Information Superhighways Revisited: The Economics of Multimedia (Boston: Artech House, 1996), pp. 228, 231.

<sup>33</sup> Ibid.

right to know what they are paying to support universal service, and it is equally important that consumers know when they are the beneficiaries of support that is provided by others. The DCA has consistently urged the CPUC and the FCC to take the high road, albeit perhaps a more difficult path, and give both the paying and receiving consumers the information they need and deserve regarding universal service programs.

Now may be the only time that a carefully-designed process can be put in place. Once the state and federal universal service systems are in place, it will be as difficult to revamp them as it has been difficult to revamp other major social initiatives. At this point in the evolution of telecommunications, the U.S. is fashioning a process that could prove to be as large and inappropriate as the tax subsidy to housing (a \$85 billion program that mainly benefits the most affluent), support to agriculture that goes mainly to large farming organizations, or a deposit insurance program that necessitated the very taxpayer bailout that the president who signed the bill adopting it predicted.

The DCA's appraisal is that from both consumer and societal standpoints, the explicit, disclosed, customer surcharge is the preferred option. While there are many reasons in support of this, the concept of openness of government decides the issue. Making the subsidy explicit to those paying it as well as those receiving it helps to keep things in the open and provides the best opportunity for correction where needed.

#### **B. The Universal Service Process Must be Efficient.**

The reason that the universal service process must be efficient is that it is clearly not the only strategy designed to serve consumers, and it has the potential to interfere with other, more viable, strategies that serve consumers.

In this new, dynamic telecommunications environment, it is the market and not universal service mechanisms that will be the chief force that fosters innovation, diversity, enhanced services and lower prices. In telecommunications, just as in consumer electronics and computers, the competitive market will support universal service goals, including affordability. If it is allowed to do so, it will achieve the same goals through advancements in technology and mass production and distribution -- a process that has placed an affordable color TV in virtually everyone's home.

There are good public policy reasons for allowing and fostering the emergence of a competitive market for telecommunications services. There also are good public policy reasons for fostering universal access to telecommunications services, which are increasingly essential as the Information Age unfolds. Those include:

- 1) the benefits to every customer of being able to connect with other people, businesses and government;<sup>34</sup>
- 2) enabling providers to make the most efficient use of large fixed plant;<sup>35</sup> and,
- 3) providing a broader showcase for new services, equipment and applications.<sup>36</sup>

In adopting the Telecommunications Act of 1996 ("the Act"), Congress recognized that in order to achieve the most optimally functioning telecommunications process, some level of government intervention, including subsidies to low-income and high-cost customers, are necessary. But since "there are fundamentally only two types of local telephone company subscribers, those providing net subsidies ("subsidizers") and those receiving subsidies

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<sup>34</sup> The value of telecommunications services to individual customers who purchase and fully pay for the services increases with the number of customers on the network. It is self-evident that the value of one's telephone is influenced by the number of persons one can call, and from whom one can receive calls, and that this is a value for which there is some monetary equivalent. Increasing the number of persons who can be reached by telephone, and who place calls themselves, also increases both telephone usage and company revenues, with additional benefits to all customers. "There is value just in having people connected to a network, the so-called network externality argument." (Blackman, Colin R., "Universal Service: Obligation or Opportunity?", Telecommunications Policy (1993, Vol. 19, No. 1), 167-176, at p. 173.) Indirect value to each customer includes the value to government and other public and private organizations whose operations are facilitated by the widespread deployment of telephone services, which redounds to the economic benefit of virtually everyone. This is a quality that markets for most other consumer products and services do not have.

<sup>35</sup> Maximizing participation by customers who can be added to the network at relatively little marginal cost makes the most efficient use of fixed plant. In this industry, there are enormous fixed costs, and often also significant excess capacity. Therefore, there are valid economic reasons to maximize usage by selling services to additional customers at rates that would be "below cost" if those additional customers did not purchase the services. Experts agree that there is "tremendous cost pressure to cut price and/or add service to fill up capacity." (Porter, Michael E., "On thinking about deregulation and competition," in Sapolsky, Harvey M., et al, eds., The Telecommunications Revolution: Past, Present, and Future (London and New York: Routledge, 1992), 40.) Given freedom to set their own prices, telecommunications service providers have a strong incentive to exercise their pricing flexibility in ways that will enhance usage to its optimum (most cost-efficient) level. Moreover, "the uneconomic customer of today may well turn out to be a competing operator's economic customer tomorrow" with the result that "providing universal service is not an obligation at all but rather an opportunity and a privilege." (Blackman, Colin R., "Universal Service: Obligation or Opportunity?", telecommunications Policy (1995, Vol. 19, No. 1), 167-176, at p. 173.)

<sup>36</sup> Fostering a "universal market" for new applications, related customer premises equipment, information services and other telecommunications services provides a broader "showcase" for the sale of those services, which in turn reduces the cost of those services for everyone. It is very difficult to transform a new, innovative and genuinely useful product or service into a profitable one, and access to the necessary "critical mass" of customers can be extremely important. (See Egan, Bruce L., "Building Value Through Telecommunications: Regulatory Roadblocks on the Information Superhighway, Telecommunications Policy (1994), 573-587, at p. 576.) Achieving broad universal service is much like laying down the country's web of freeways: a huge volume of commerce among widely disparate geographical areas would not exist today but for the foundation of the interstate freeway and highway systems.