Decision **DRAFT DECISION OF ALJ JONES** (Mailed 4/2/2002)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Roseville Telephone Company (U 1015 C) to Review Extended Area Service Compensation and Establish Replacement Revenue Funding.	Application 99-08-043 (Filed August 20, 1999)

OPINION DENYING PETITION TO MODIFY

1. Summary

In this decision we deny Roseville Telephone Company's (Roseville) Petition to Modify Decision (D.) 00-11-039 and uphold our determination in D.00-11-039 that the California High Cost Fund-B (CHCF-B) is not an appropriate permanent source of funding to replace the $11.5 million Extended Area Service (EAS) payment Roseville previously received from Pacific Bell Telephone Company (Pacific).

2. Background

D.00-11-039 discontinued Pacific's EAS payments to Roseville and provided Roseville with interim funding from the CHCF-B pending a subsequent investigation into the manner in which permanent replacement of EAS payments will be addressed. In that decision, we denied Roseville's request to use the CHCF-B as a permanent source of funding to replace the $11.5 million payment from Pacific. (D.00-11-039 at 46.) On May 4, 2001, Roseville filed a Petition for Clarification/Modification of D.00-11-039; the Office of Ratepayer Advocates (ORA) filed its Response on June 4, 2001.

3. Roseville's Petition for Modification

Roseville requested two things in its Petition. It asked the Commission to clarify the language in four areas of D.00-11-039, and to modify the decision to allow use of the CHCF-B as a permanent means of revenue recovery for Roseville. Roseville's requests for clarification and modification are addressed separately below:

3.1 Request for Clarification: Conformance with Principles Underlying CHCF-B

According to Roseville, D.00-11-039 makes a number of statements that contradict the fundamental characteristics of the CHCF-B. Roseville believes that these statements could be misinterpreted and constitute legal error in that they overturn prior Commissions, e.g. D.96-10-066, without notice and opportunity to be heard by Roseville, as well as other affected parties. The four specific sections Roseville alludes to are each addressed below:

3.1.1 Page 46 of the decision states:

> In fact, Roseville's proposal would completely change the character of the CHCF-B from a system of support for CBGs [census block groups] in high cost areas. Roseville would turn the fund on its head and make it the source of a subsidy to Roseville, which we clearly never intended and will not entertain at this time.

According to Roseville, contrary to this statement, the CHCF-B currently is and has for many years been a source of support to Roseville, as well as to other incumbent local exchange carriers (ILECs). Additionally, the support is not and never has been provided to CBGs, but to local telephone companies on the basis of Pacific's cost proxy model's cost calculations that are performed with respect to the characteristics of CBG areas they serve. The main point is that the CHCF-B was established to keep basic service rates reasonable and affordable.

In its Response, ORA states that Roseville misunderstands the fundamental purpose of the CHCF-B, which is to ensure that residential telephone basic service rates remain affordable in high cost areas. Roseville, along with other ILECs currently receives financial support from the CHCF-B to achieve that purpose.

Roseville, however, also requests that it be permitted to draw $11.5 million on an annual basis from the CHCF-B to replace the EAS revenues that it no longer receives from Pacific, in addition to the approximately $500,000 it receives to provide residential basic service at affordable rates in high cost areas. ORA asserts that the Commission denied Roseville's request because the CHCF-B was never intended to be used for non-Universal Service purposes such as EAS.

We find that Roseville has taken this language out of context and assigned it a meaning we never intended. We are certainly aware that payments are made to telecommunications carriers who serve high cost CBGs, not to the CBGs themselves. In fact, the paragraph above the one cited by Roseville, states that fact very clearly. We quote:

> Further, ORA is correct in noting that the Commission specifically limited the scope of the CHCF-B *to carriers providing residential local exchange service in high-cost areas.* (Emphasis added.)

In addition, the paragraph Roseville cites does not say that payments are *made* to CBGs, merely that the CHCF-B provides a system of support *for* CBGs in high cost areas, which is indeed the case. The CHCF-B provides a system of support for carriers who serve high cost areas. Roseville's request for clarification of the language on page 46 of D.00-11-039 is denied.

3.1.2 Roseville cites the following from page 60 of D.00-11-039:

> In today's competitive environment, a competitor in the telecommunications market should not have the advantage of an outside subsidy to fund its operations.

According to Roseville, this statement contradicts the fundamental nature of the CHCF-B, as well as the Public Utilities Code and the Federal Telecommunications Act of 1996 (TA96), which call for open local competition along with a system of universal service support that makes all subsidies explicit. Roseville asserts that this statement would appear to require that the Commission discontinue the CHCF-B in its entirety because each carrier that currently receives CHCF-B support is a competitor that receives an external subsidy that, by the nature of receiving this support, funds its operations.

ORA responds that Roseville's interpretation of this statement is flawed because it is taken out of context. According to ORA, nothing in the statement suggests that the Commission intended to discontinue the CHCF-B in its entirety. Rather, as is apparent from a reading of the statement in the context of the decision in its entirety, the Commission intended that Roseville should not be permitted to receive subsidy from the CHCF-B to replace the EAS revenues because no other ILECs are permitted to fund their operations in such a manner. Hence, if Roseville were permitted to use the CHCF-B to replace the EAS revenues, it would have the advantage of an outside subsidy that is not afforded to other ILECs.

We find that, once again, Roseville has taken language of D.00-11-039 out of context. We cite the entire paragraph that includes the sentence Roseville quoted to show the correct context for our remark:

> NRF [New Regulatory Framework] is the cornerstone of our regulation of all large and mid-sized LECs in California, and we do not intend to change that. However, in the case of

> Roseville, we need to recalibrate Roseville's revenue requirement to determine whether Roseville is able to absorb some or all of the $11.5 million or whether the revenue must come from Roseville's ratepayers. Our ultimate goal is to have Roseville dependent on its own resources for its revenue requirement. *In today's competitive environment, a competitor in the telecommunications market should not have the advantage of an outside subsidy to fund its operations.* (Emphasis added.)

This paragraph clearly focuses on the recovery of the $11.5 million EAS payment, and has nothing to do with Roseville's draws from the CHCF-B as a result of serving high cost areas. Also, the payments ILECs receive from the CHCF-B for serving high cost areas do not constitute an additional outside subsidy, since those carriers must reduce their rates by the same amount as their draws from the CHCF-B. California's universal service program, and the payments ILECs receive from the CHCF-B are not within the scope of this proceeding. The proceeding dealt exclusively with Roseville's recovery of the $11.5 million EAS payment. If the language Roseville cites is placed in context with the rest of the paragraph, the meaning is perfectly clear. Roseville's request to have this statement deleted is denied.

3.1.3 Roseville cites the following statement on page 66 of D.00-11-039:

> We are serious about moving this OII [Order Instituting Investigation] forward so that we can eliminate the California ratepayer subsidy of Roseville's operations, and we will commit the necessary Commission resources to completing the OII as quickly as possible.

According to Roseville, this statement implies that the Commission intends to end the current payments Roseville receives from the CHCF-B as a result of CBG-related cost calculations. Additionally, combined with the statements referenced above about an incompatibility between competition and CHCF-B subsidy, this language seems to raise an equal protection concern as to

why the Commission would seek to eliminate subsidy support for only one carrier, Roseville. Roseville recommends that the Commission delete this statement from D.00-11-039.

ORA responds that Roseville's interpretation of the statement is flawed. The statement cited above appears in D.00-11-039 in the context of the Commission's decision to provide interim relief to Roseville. The Commission ruled that Roseville should be allowed to receive $11.5 million on an interim basis from the CHCF-B until the OII into Roseville's revenue requirement is completed. Thus, by this statement, the Commission merely states that the OII should move forward quickly so that the interim relief for the EAS revenues is eliminated and a permanent solution is achieved. According to ORA, the Commission does not imply that Roseville would no longer receive support from the CHCF-B to provide residential basic service in high cost areas.

We agree with ORA's conclusion that Roseville quoted language out of context. This particular section of D.00-11-039 deals with the "next steps" we intended, namely an OII to examine Roseville's expense levels and revenue requirement to determine the appropriate funding source to replace the $11.5 million EAS payment which Roseville previously received from Pacific and now receives, on an interim basis, from the CHCF-B.

We reiterate that the payments Roseville or any other ILEC receive from the CHCF-B for providing service in high cost CBG areas are outside the scope of the proceeding. Nothing in D.00-11-039 should be construed to impact on the approximately $500,000 which Roseville currently receives from the CHCF-B for providing service in high cost areas within its service territory.

There is no need for clarification, if the sentence Roseville cited is read in the proper context. Roseville's request to have this statement deleted is denied.

3.1.4 According to Roseville, Finding of Fact 1 is also potentially problematic. It reads as follows:

1. It is not sustainable in a competitive environment for one company to make subsidy payments to its competitor.

Roseville asserts that under the current operations of the CHCF-B, Roseville makes substantial payments to its competitors, including Pacific. In fact, Roseville claims that many companies make payments into the CHCF-B to fund other competitor company operations. This statement could be misinterpreted to conclude that CHCF-B payments are not sustainable in a competitive environment as such contributions to a fund provide support to a competitor's operations. For this reason, Roseville recommends deleting Finding of Fact 1.

ORA responds that Finding of Fact 1 must be viewed in the context of EAS, not in the context of CHCF-B distributions. According to ORA, the statement correctly points out that requiring Pacific to continue to make EAS payments to Roseville is not sustainable in a competitive environment because no other ILECs have similar EAS arrangements. Both Citizens Telecommunications Company of California and GTE California ended their EAS arrangement with Pacific in 1997.

We find that Roseville's attempt to compare EAS payments to CHCF-B payments is a case of mixing apples and oranges. The important distinction is the source of the money for the EAS and CHCF-B payments. While Roseville seems to indicate that Roseville itself is making payments to other carriers under CHCF-B rules, those payments to the CHCF-B do not come from Roseville's own revenues, but from its ratepayers, in the form of a surcharge assessed on customers' bills. Roseville merely aggregates the payments and sends those payments to the CHCF-B for distribution. On the other hand, the EAS payment

that Pacific previously made to Roseville was not paid by Pacific's customers in the form of a surcharge. The payment came from Pacific's resources, and it is exactly this form of payment that is not sustainable in a competitive environment. Finding of Fact 1 refers to the EAS payment at issue here, namely a payment out of one company's pocket that goes into a competitor's pocket. On that basis, we decline to delete Finding of Fact 1.

We disagree with Roseville's assertion that the four sections from D.00-11-039 could be misinterpreted and constitute legal error. Reading those sections in the proper context shows that they not overturn prior Commission decisions (e.g., 96-10-066). Nor are they contrary to Public Utilities Code Section 739.3 or Section 254 of the Telecommunications Act of 1996 (TA96). D.96-10-066, § 739.3, and § 254 of TA96 all deal with universal service issues, including the CHCF-B. Those sections have nothing to do with the issue which is the core of this proceeding, namely a permanent funding source for recovery of the $11.5 million in EAS payments which Roseville previously received from Pacific.

3.2 Request for Modification: Use of the CHCF-B as a Source of Replacement Revenues

Roseville asserts that the Commission should not preclude use of the CHCF-B, either in whole or in part, to help keep Roseville's rates affordable into the future. Roseville believes its costs are reasonable and that the entirety of the $11.5 million will be acknowledged as appropriate for ongoing recovery. In that case—or even in the case where only partial recovery might be permitted—Roseville continues to believe that a source of support like the CHCF-B may be necessary to avoid substantial increases to residential rates that are already among the highest in the state.

Roseville believes the Commission is exercising good judgment in using the CHCF-B as a support source for the temporary payments while the OII is underway, and D.00-11-039 confirms the legality and reasonableness of this step. Just as the Commission chose to use the CHCF-B at this time in lieu of large rate increases to Roseville's customers, so may the Commission wish to do the same in the future when the OII is completed and a permanent solution must be found. The decision to raise rates substantially will not become any easier between now and the time that the OII concludes. Roseville requests that D.00-11-039 be modified to indicate that parties may raise the continued use of the CHCF-B as an option for consideration in the OII.

In its Response to Roseville's Petition, ORA asserts that the issue of whether the CHCF-B is an appropriate source of replacement funding for the EAS revenues has been fully litigated and resolved by the issuance of D.00-11-039, and Roseville should not now be allowed to re-litigate this issue. The Commission denied Roseville's request to recover its EAS revenues through the CHCF-B.

ORA states that if the Commission nonetheless determines that it will consider reversal of the decision to allow the CHCF-B to be used as a potential source of replacement funding, the Commission should defer the issue to the Universal Service triennial review. The purpose of the review is to examine various programs, including the CHCF-B. The issue of whether the CHCF-B program should be modified to allow Roseville to make a permanent draw of $11.5 to replace the EAS revenues should be considered, if at all, in that proceeding.

We stand by our determination in D.00-11-039 that the CHCF-B is not an appropriate permanent source of funding to replace the $11.5 million payment

from Pacific. Following is a summary of the reasons we listed in D.00-11-039, which still hold true today:

First, since the CHCF-B is funded from a statewide surcharge on all telephone ratepayers in California, Roseville is asking to have its operations subsidized by other California ratepayers. Under Roseville's proposal, the subsidy would be permanent, and not subject to any further scrutiny.

Also, the CHCF-B as formulated in 1996 does not provide any new money to carriers. Any carrier, including Roseville, which receives a draw from the CHCF-B must reduce its rates by the same amount. Further, ORA is correct in noting that the Commission specifically limited the scope of the CHCF-B to carriers providing residential local exchange service in high-cost areas. (*See* D.96-10-066, Ordering Paragraphs 7 and 8.)

Roseville acknowledges that significant changes would have to be made to the CHCF-B in order for it to be used for permanent draws of a fixed amount. In fact, Roseville's proposal would completely change the character of the CHCF-B from a system of support for CBGs in high cost areas. Roseville would turn the fund on its head and make it the source of a subsidy to Roseville, which we clearly never intended and will not entertain at this time.

Comments on Draft Decision

The draft decision of ALJ Jones in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7.

Findings of Fact

1. Roseville has taken language of D.00-11-039 out of context and assigned it meanings not intended by the Commission.

2. The second full paragraph on page 60 of D.00-11-039 focuses on the recovery of the $11.5 million EAS payment, and has nothing to do with Roseville's draws from the CHCF-B as a result of serving high cost areas.

3. Payments ILECs receive from the CHCF-B for serving high cost areas do not constitute a subsidy as those carriers must reduce their rates by the same amount.

4. A.99-08-043 dealt exclusively with Roseville's recovery of the $11.5 million EAS payment Roseville previously received from Pacific, and did not address any changes to operation of the CHCF-B.

5. Payments Roseville makes to the CHCF-B do not come from Roseville's resources, but from its ratepayers, in the form of a surcharge assessed on customers' bills.

6. The EAS payment that Pacific previously made to Roseville came from Pacific's resources.

7. The CHCF-B as formulated in D.96-10-066 does not provide any new money to carriers. Any carrier that receives a draw from the CHCF-B must reduce its rates by the same amount.

Conclusions of Law

1. D.00-11-039 does not overturn or modify D.96-10-066.

2. The four sections of D.00-11-039 that Roseville cited do not constitute legal error.

3. Roseville's requests for clarification of language in D.00-11-039 should be denied.

4. The CHCF-B is not an appropriate permanent source of funding to replace the $11.5 million payment to Roseville from Pacific.

5. Significant changes would have to be made to the CHCF-B in order for it to be used for permanent draws of a fixed amount.

6. Roseville's request for modification of D.00-11-039 should be denied.

O R D E R

IT IS ORDERED that Roseville Telephone Company's Petition for Clarification/Modification is denied.

Dated _____, at San Francisco, California.