BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into the Review of the California High Cost Fund-A Program.	FILED PUBLIC UTILITIES COMMISSION NOVEMBER 10, 2011 SAN FRANCISCO, CALIFORNIA RULEMAKING 11-11-007

ORDER INSTITUTING RULEMAKING REGARDING CALIFORNIA HIGH COST FUND-A PROGRAM

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1. Introduction

With this Order Instituting Rulemaking (OIR), the Commission begins a review of the California High Cost Fund-A (CHCF-A) program. This OIR was issued pursuant to the Commission's Decision (D.) 10-02-016.[1] A detailed review of the program is warranted in response to market, regulatory, and technological changes since the California High Cost Fund program was first established in 1987. In this OIR, we seek comment on how the program can more efficiently and effectively meet its stated goals. To the extent deficiencies are identified, we solicit constructive proposals on whether the program should continue and if so, how should it be modified.

In Order Instituting Rulemaking (R).06-06-028 and the resultant D.07-09-020,[2] the Commission recognized that the California telecommunications market has significantly changed since the last modifications were made to the high cost fund programs. When the High Cost Fund programs were created over two decades ago, landline telephone service was the only widely-available form of affordable telecommunications technology. Now consumers are increasingly communicating in ways other than through traditional landline

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[1] D.10-02-016 Ordering paragraph 4: The Communications Division shall draft an Order Instituting Rulemaking for our consideration to be placed on the Commission's agenda within 90 days of the effective date of this decision to address all relevant issues regarding high-cost support for Small Local Exchange Carriers.

[2] R.06-06-028, Order Instituting Rulemaking into the Review of the California High Cost Fund B Program. D.07-09-020, Interim Opinion Adopting Reforms to the High Cost Fund-B Mechanism.

telephones. For example, in 1987 there were less than 900,000 wireless subscribers in the entire country.[3] By the end of 2000, wireless subscribership in America exceeded 100 million and digital wireless users outnumbered analog subscribers.[4] By June of 2010, there were approximately 293 million wireless subscribers in the U.S. who now also use their wireless devices to access other services such as text messaging[5] (see Appendix A), email, internet access, and other data applications. In addition to wireless technologies, Internet-based communications including Voice over Internet Protocol (VoIP) have become widely available and have greatly expanded the range of affordable telecommunications services offered to consumers in California.

In this context, the CHCF-A program should be modified to reflect the modernization of telecommunications services. Furthermore, the current CHCF-A subsidy mechanism now faces new challenges since major Incumbent Local Exchange Carriers' (ILECs) rates became fully deregulated in 2011. We must determine whether the program remains necessary to achieve the fundamental statutory goal of enhancing universal service and, if so, what changes are necessary to further this goal in today's telecommunications environment where varied technologies compete to fulfill the communication needs of consumers.

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3 CTIA Survey Mid Year 2010.

4 http://www.ctia.org/media/industry_info/index.cfm/AID/10392.

5 CTIA Survey Mid Year 2010.

The CHCF-A is funded by a surcharge assessed on an end-user's billed intrastate telecommunications services, therefore we have an obligation to ensure that the funds obtained from ratepayers are being spent wisely.[6] To this end, this rulemaking seeks comment on several questions, including the following fundamental question:

What is the most appropriate, efficient, and effective means of minimizing rate disparity and promoting California's goal of providing universal service?[7]

2. Background

The CHCF-A is a subsidy program based on the principle of universal service. Universal service as it applies to telecommunications services is the concept that consumers should have access to basic telephone service in their homes that is both affordable and ubiquitously available. Legislatures have codified this policy, finding that as more citizens are connected to the telecommunications network, the value of the network grows. Thus, it has been a longstanding commitment of federal and state governments to promote policies that encourage universal telecommunications service.[8]

With this in mind, a review of the CHCF-A should first begin with a review of the original purposes and goals of the program, as articulated in statutes and in our decisions adopting the program. We will briefly review the federal and state legislative history of universal service to provide a background for this review.

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[6] Public Utilities (Pub. Util.) Code § 709.

[7] See D.07-09-020, *Interim Opinion Adopting Reforms to the High Cost Fund-B Mechanism*, Ordering Paragraphs (OP) 6 and 7.

[8] See Pub. Util. Code § 709; 47 U.S.C. §§ 151, 254.

2.1. Federal Legislative History

The United States Congress made universal service a basic goal of telecommunications regulation with the passage of the Communications Act of 1934. Section 1 of this act created the Federal Communications Commission (FCC):

> [f] or the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges . . . .[9]

In 1996, Congress passed the Telecommunications Act of 1996 (1996 Act). This was the first major overhaul of telecommunications policy in nearly 62 years and it modified earlier telecommunications legislation, primarily the Communications Act of 1934. The 1996 Act codified the FCC's longstanding practice of providing universal service support for "telecommunications services" in high cost and low income areas. The 1996 Act also defined the nature of "universal service" as "an evolving level of telecommunications services" that takes into account telecommunications service advancements. Additionally, it established that consumers in rural, insular, and high cost areas should have access to telecommunications services at rates that are "reasonably comparable to rates charged for similar services in urban areas."[10] Further, this

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[9] 47 U.S.C. § 151 (as amended).

[10] 47 U.S.C. § 254(b) (3).

Act provided a list of principles upon which the FCC must base policies for the preservation and advancement of universal service.[11]

With respect to the states' authority to regulate universal service, the 1996 Act maintained and confirmed state regulatory authority to impose, on a competitively neutral basis, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers.[12]

2.2. California Legislative History

In 1987, the California legislature enacted Pub. Util. Code § 739.3 requiring the Commission to develop, implement, and maintain a suitable program to establish a fair and equitable local rate structure aided by transfer payments to small independent telephone companies serving rural and small metropolitan areas.[13] The purpose of the program is to, "promote the goals of universal telephone service and to reduce any disparity in the rates charged by

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[11] 47 U.S.C. § 254(b) (1)-(7). The principles are (1) Quality services should be available at just, reasonable, and affordable rates; (2) Access to advanced telecommunications and information services should be provided in all regions of the nation; (3) Consumers in all regions of the state should have access to telecommunications and information services, including advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and reasonably comparable to rates charged for similar services in urban areas; (4) All providers of telecommunications services should contribute in an equitable and nondiscriminatory manner; (5) Federal and State support mechanisms must be specific, predictable and sufficient to preserve and advance universal service; (6) Schools, libraries, and rural health care providers should have discounted access to advanced telecommunication services; and (7) Any other principles as the Joint Board and the FCC determine are necessary and appropriate – which the FCC used to add a competitive neutrality requirement.

[12] 47 U.S.C. § 253 (b).

[13] Pub. Util. Code § 739.3(a); Assembly Bill 1466 (Chapter 755, Statutes of 1987).

those companies" in comparison to the lower rates charged to customers in larger metropolitan areas.[14]

In response to the Legislature's mandate, the Commission established the original High Cost Fund to provide a source of supplemental revenues to small and mid-size ILECs whose basic exchange access line service rates would otherwise be increased to levels that would threaten universal service.[15] The original program was funded by an increment in Pacific Bell's intrastate carrier common line charge and was administered by Pacific Bell. In 1994, the Commission changed the funding source from an increment in the carrier common line charge to a surcharge paid by all end-users, and reaffirmed Pacific Bell as the administrator of the fund.[16]

Addressing the emergence of competition for local exchange services, in 1996, the Commission decided that in addition to support for small and medium sized carriers, mechanisms needed to be established that would support

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[14] D.85-06-115 as modified by D.88-07-022, D.88-12-044 and D.91-09-042. The California High Cost Fund (i.e. the current CHCF-A) was implemented by D.88-07-022 as modified by D.91-05-016 and D.91-09-042 to provide a source of supplemental revenues to three mid-size and seventeen small Local Exchange Carriers whose basic exchange access line service rates would otherwise be increased to levels that would threaten universal service. D.96-10-066 changed the name of the High Cost Fund to CHCF-A and created the California High Cost Fund-B (B-Fund). This decision included the three mid-size LECs in the B-Fund program for the purpose of determining universal service subsidy support and maintained the CHCF-A for the 17 small Local Exchange Carriers. CHCF-A is funded by a surcharge assessed on consumers' intrastate telecommunications services.

[15] D.88-07-022 (as modified by D.91-05-016 and the Appendix in D.91-09-042) provides the implementation guidelines for the California Intrastate High Cost Fund.

[16] D.94-09-065, Re: Alternative Regulatory Frameworks for Local Exchange Carriers, Section XIII.D.1.c and OP 71.

universal service in high-cost areas served by the large ILECs. Recognizing that small ILECs should not be subject to the same rules applicable to the larger ILECs,[17] in 1996 as the Commission changed the name of the original High Cost fund to CHCF-A, it created the California High Cost Fund B (CHCF-B) to provide high cost support for the large carriers; i.e. Pacific Bell (now dba AT&T of California), GTE California and GTE Contel (now Verizon California[18]), Roseville Telephone Company (now SureWest), and Citizens Telecommunications Company of California (now Frontier Communications of California[19]).[20] The Commission began administering the CHCF-A program for eligible small ILECs,[21] relieving Pacific Bell of the responsibility.

In 2008, the Legislature further added Pub. Util. Code § 275.6(d) and amended Pub. Util. Code § 739.3(h) The legislation required the Commission to prepare and submit to the Legislature a report on the affordability of basic

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17 D.96-10-066, Order Instituting Rulemaking (OIR or R.) 95-01-020, Investigation on the Commission's Own Motion into Universal Service and to Comply with the Mandates of Assembly Bill 3643, Ordering Paragraphs 8 and 9.

18 Referred to in this document as "Verizon."

19 Referred to in this document as "Frontier."

20 MCI and Cox Communications have subsequently been added as CHCF-B carriers.

21 D.96-10-066, Attachment A to Appendix B. At the time, there were seventeen small LECs as follows: Calaveras Telephone Company, California-Oregon Telephone Company, Citizens Telecommunications Company of the Golden State, Citizens Telecommunications Company of Tuolumne , Ducor Telephone Company, Evans Telephone Company, Foresthill Telephone Company, GTE West Coast Incorporated, Happy Valley Telephone Company, Hornitos Telephone Company, Kerman Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Siskiyou Telephone Company, Volcano Telephone Company, and Winterhaven Telephone Company.

telephone service in areas funded by the CHCF-B.[22] The sunset of CHCF-A and CHCF-B programs is now extended to January 1, 2015.[23]

2.3. Current Status of the CHCF-A

The CHCF-A is funded by an all-end-user surcharge, assessed as a percentage of all customers' intrastate service charges (other than LifeLine services). The surcharge is revised as needed to ensure adequate funding. The surcharge rate is based on the program's total funding requirement (i.e., sum of all participating carrier's funding requirements) divided by the total projected intrastate revenue subject to surcharge.

Initially, 17 carriers were eligible to apply for the CHCF-A funding. Subsequently, D.08-10-010 authorized Citizens Telecommunications Company of California, Inc. to consolidate with three CHCF-A eligible small ILECs: Citizens Telecommunications Company of Tuolumne, Citizens Telecommunications Company of the Golden State and Global Valley Networks, Inc. This consolidation resulted in a reduction in the total number of small ILECs eligible for CHCF-A support from 17 to 14. This reduction did not impact the CHCF-A as these carriers were not drawing from the fund at the time.

Carriers' funding requirements for the CHCF-A are determined through General Rate Cases (GRCs). Carriers have the option to take the informal path of filing an advice letter or go through a formal application process. The informal GRC advice letter filings for small ILECs are typically reviewed by the Communication Division (CD). The process requires CD to review the filing company's estimated revenues, expenses, rate base and rate of

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22 Senate Bill (SB) 780, Chapter 342, approved September 26, 2008.

23 SB 3, Chapter 695, approved October, 9, 2011.

return in order to arrive at an appropriate revenue level necessary for operation. Subsequently, CD prepares a resolution for the Commission to authorize the ongoing funding level in response to annual carrier funding request advice letters.

In the formal application process however, the application is assigned to an Administrative Law Judge (ALJ) with the carrier and the Division of Ratepayers Advocates (DRA) identified as parties to the proceeding. In the application process, DRA reviews the carrier filings as CD does in the informal process and testifies on its findings. The ALJ can use CD's resources to review application details independent of the parties. Subsequently, the ALJ drafts a decision for the Commission to vote on and to authorize the recommended funding level.[24]

The Commission uses the revenue requirement derived from GRCs to determine appropriate rates for telecommunications services, up to 150%[25] of the rates of comparable services in urban areas.[26] If carriers cannot meet their revenue requirement with these maximally allowed rates, they are granted the CHCF-A subsidy to cover the shortfall. The CHCF-A funding level for each carrier is the difference between the revenue requirement and the carrier's actual revenue. The CHCF-A support is then distributed to carriers directly on a monthly basis.

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[24] http://docs.cpuc.ca.gov/word_pdf/RULES_PRAC_PROC/105138.pdf.

[25] D.91-09-042 limited High Cost Fund subsidy to only those services above 150% of urban rates.

[26] D.10-02-016 set AT&T's basic rate as the proxy for urban rates.

Appendix B shows the Commission-approved CHCF-A support to the small ILECs. Appendix C shows the intrastate revenue requirement amounts these carriers requested from the CHCF-A for the years 1998 through 2010. The difference between a small ILEC's revenue requirement request (Appendix C) and the Commission-approved CHCF-A support (Appendix B) is caused by the application of the means test and the applicable "waterfall" decrement if any, for each small ILEC.[27] [28] Appendix D shows the number of access lines by each small ILEC as of 2010. The current surcharge for the CHCF-A is 0 percent as of December 2010. The history of the CHCF-A surcharge is shown in Appendix E. The fiscal year 2012-2013 budget is $$49.77 million.[29]

3. Developments That May Impact the CHCF-A

Changes of rules and regulations at the federal and state level are expected to affect the CHCF-A program in coming years. The following are developments that should be monitored for their potential impacts.

3.1. Federal High Cost Fund

On October 27, 2011, the FCC approved the creation of Connect America Fund (CAF) to help extend high speed internet to unserved Americans. This major policy decision also intends to comprehensively reform its Universal

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[27] For means testing Small LECs' CHCF-A support is limited to forecasted intrastate results of operations not to exceed the small LEC's authorized rate of return. The forecasted earnings are based on at least seven months of recorded financial data.

[28] The waterfall provision refers to the 6-year phase down of CHCF-A funding level beginning in the year after the completion of a GRC. The funding levels are 100% of the CHCF-A amount for the first three years, 80% the fourth year, 50% the fifth year, and 0% thereafter.

[29] The Resolution T-17331.

Service Fund and intercarrier compensation systems because the FCC believes "these systems have been widely viewed as broken, and long overdue for reform."[30] One of the goals of this reform among other things is the commitment to fiscal responsibility of the newly created CAF. A firm annual budget set at current levels—$4.5 billion—will prevent growth in the Fund and help protect consumers from increased contribution fees. Programs that provide subsidies where they are not needed are eliminated, and compensation for corporate overhead expenses is reduced. Market-based mechanisms, including competitive bidding, will be used to distribute money more efficiently.[31] Additionally, the FCC adopts reforms to: (1) establish a framework to limit reimbursements for excessive capital and operating expenses, which will be implemented no later than July 1, 2012, after an additional opportunity for public comment; (2) encourage efficiencies by extending existing corporate operations expense limits to the existing high-cost loop support and interstate common line support mechanisms, effective January 1, 2012; (3) ensure fairness by reducing high-cost loop support for carriers that maintain artificially low end-user voice rates, with a three-step phase-in beginning July 1, 2012; (4) phase out the Safety Net Additive component of high-cost loop support over time; (5) address Local Switching Support as part of comprehensive ICC reform; (6) phase out over three years support in study areas that overlap completely with an unsubsidized facilities-based terrestrial competitor that provides voice and fixed broadband

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30 The FCC News Release October 27, 2011. http://transition.fcc.gov/Daily_Releases/Daily_Business/2011/db1027/DOC-310695A1.pdf

31 Ibid.

service, beginning July 1, 2012; and (7) cap per-line support at $250 per month, with a gradual phasedown to that cap over a three-year period commencing July 1, 2012.[32]

We believe Federal proceedings have the potential to affect state programs. The largest and most immediate potential effect will be an increase of draws from the CHCF-A by small ILECs. This will cause an added financial burden to the California ratepayers, if CHCF-A rules stay unchanged.[33]

The Commission has noticed that the CHCF-A carriers have more heavily invested in plant modernization, including switching to broadband capable fiber optic networks, than their counterpart carriers that did not receive the support funds. The FCC reforms are of particular interest to California because under the current rules, any reduction in federal high cost support translates into an increase in support from the CHCF-A. The state's subsidy mechanisms should be addressed now, as the potential effects of federal funding mechanism changes could result in a substantial impact to the CHCF-A program.

On April 21, 2010 the FCC issued a Notice of Inquiry and Notice of Proposed Rulemaking through which FCC sought comments on, among other things, how to cap and cut inefficient funding in the high cost mechanisms and to shift savings toward broadband communications. The FCC has determined that current high cost programs are less than "economically efficient" in providing support. We believe this Federal action will most likely affect state programs. The largest and most immediate potential effect will be an increase of

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[32] Ibid., at 2-7.

[33] FCC, FCC 10-58 http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-10-58A1.pdf.

draws from the CHCF-A by small ILECs. This will cause an added financial burden to the California ratepayers, if CHCF-A rules stay unchanged.[34]

3.2. National Broadband Plan

In early 2009, Congress directed the FCC to develop a National Broadband Plan[35] that would ensure every American with "access to broadband capability." The FCC initiated the process of developing this plan with a Notice of Inquiry in April 2009. The Notice identifies a need for significant changes to the current high cost program, among which it recommends:

> cut inefficient funding of …voice service[through high cost mechanisms] and refocus universal service funding to directly support modern communications networks that will provide broadband as well as voice services.[36]

The FCC contends "the intent [of revisions in high cost support mechanisms]… is to eliminate the indirect funds of broadband-capable networks today through our legacy high-cost programs which is occurring without transparency or accountability for the use of funds to extend broadband service."[37]

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[34] FCC, FCC 10-58 http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-10-58A1.pdf.

[35] http://www.broadband.gov/.

[36] FCC, *Connecting America: The National Broadband Plan*, 147-48 (rel. Mar. 16, 2010) (National Broadband Plan).

[37] FCC 10-58, In the Matter of Connect America Fund A National Broadband Plan for Our Future High-Cost Universal Service Support, at 22-23. http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-10-58A1.pdf.

capable fiber optic networks, than their counterpart carriers that did not receive the support funds. These proceedings are of particular interest to California because under the current rules, any reduction in federal high cost support translates into an increase in support from the CHCF-A. The state's subsidy mechanisms should be addressed now, as the potential effects of federal funding mechanism changes could result in a substantial impact to the CHCF-A program.

4. Current Status of the Telecommunications Market

In order to propose changes that may have profound effects on California's telecommunications market, we believe it to be appropriate that we examine the current state, and how the CHCF-A's impact has evolved over time.

4.1. The FCC Data on Trends in Telephony

Each year the FCC releases its latest data on telephony. According to the most recent report released in September 2010, the following trends are notable:

- The proportional expenditure on telephone services has remained flat. Approximately 2% of all consumer expenditures are devoted to telephone service. This percentage has remained virtually unchanged over the past 20 years, despite major changes in the telephone industry and in telephone usage. Average annual expenditures on telephone service increased from $360 per household in 1981 to $1,100 in 2008.[38] This increase can be explained by the fact that while in 1981, virtually, all telephone services were landlines, in recent years consumers have been subscribing to competitive

[38] Trends in Telephony, FCC, http://www.fcc.gov/Daily_Releases/Daily_Business/2010/db0930/DOC-301823A1.pdf, at 3-1.

technologies such as wireless cellular telephone services and VoIP. These new technologies are proving to be serious competition to traditional landline telephone service.

- Consumers spent less on landlines and more on wireless and Internet. Since the year 2000, personal expenditure on landline telephone services have declined while the cost of wireless telephone services and Internet Access Services have increased (also see Appendix F).[39]

- Growth of Wireless Telephone Services. Prior to 2000, landline growth over time averaged about 3% per year, reflecting growth in the population and economy. Since 2000, the number of lines provided by landline carriers has declined, likely due to consumers substituting alternatives for their landline service, and some households eliminating second lines when they move from dial-up Internet service to broadband service.[40] The percentage of people who only subscribed to landline service dropped from 23.8% in 2007 to 14.9% in 2009, while those with only a wireless telephone increased from 13.6% to 24.5% in the same period.[41] In 1984, there were 92,000 wireless subscribers in the U.S. In 2005, the number of wireless subscribers grew to 207 million. By the end 2008, the number had reached 270 million.[42] California experienced wireless subscription growth from 25.5 million at the end 2005 to 32.18 million at the end of 2008.[43]

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39 Ibid, Table 3.4.

40 Ibid, at 7-1.

41 Ibid, Table 7.4.

42 Ibid, Table 11.1.

43 Ibid, Table 11.2.

- Growth of Local Telephone Competition by VoIP. Since 2002, cable companies and others have begun offering retail interconnected VoIP. This service enables voice communications over a broadband connection and allows users both to receive calls from and place calls to the public switched telephone network, like traditional phone service. The service represents a rapidly growing part of the U.S. voice services market. These services include nomadic offerings from companies like Vonage and Skype as well as fixed offerings from cable and telephone companies that own their own networks.[44] At the end of June 2010, California had 7.64 million residential switched access lines for ILECs and almost 615 thousand switched access lines for Non-ILECs. For the same period, ILEC customers purchased 264,000 VoIP services from ILECs and 2.2 million VoIP services from Non-ILECs.[45]

4.2. The Commission Report on Affordability of Basic Telephone Service

The California legislature through Senate Bill 780 directed the Commission to survey the affordability of basic telephone service in areas funded by the CHCF-B. In response, the Commission ordered in D.08-09-042 a statewide affordability survey. In September 2010, the Commission released its report to the Legislature on the Affordability of Basic Telephone. Given the similarities between populations served by the CHCF-A and the CHCF-B, it is reasonable to use the findings of the Commission study done on the CHCF-B

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[44] Ibid, at 8-1.

[45] Local Telephone Competition Status As Of June 30, 2010. http://transition.fcc.gov/Daily_Releases/Daily_Business/2010/db0903/DOC-301310A1.pdf

population as a proxy to evaluate the demand for communications services in CHCF-A eligible service territories.

The following are study findings that we deem useful for this evaluation:

- California household telephone bills in 2010, after being adjusted for inflation, have not changed significantly since 2004.
- Data suggests there is a growing acceptance and use of wireless, VoIP and broadband services as a complement and/or substitute for traditional landline telephone service.
- Landline subscriptions are diminishing.
- Policies should take into account the availability and substitutability of alternative services such as wireless, VoIP and broadband services, and should be considered in any program redesign.
- Broadband service is increasingly important to households as it is the least likely service to be discontinued if bundled service rates increase.[46]

The findings of this report look to be consistent with the trends identified in the FCC's Report on Telephony. Both sets of data suggest relative stability in billed telephone expenses, and both indicate a steady decrease in the number of landline telephones in favor of new voice communications technologies such as wireless telephones and VoIP. Therefore, if at all levels i.e. federal, state, and within the CHCF-B territories comparable trends are observed,

[46] Staff Report to the California Legislature: Affordability of Basic Telephone Service, September 30, 2010. http://www.cpuc.ca.gov/NR/rdonlyres/383BBEA3-45F8-42E4-8582-70413539AC45/0/2010_Affordability_Report_Final_Sep_29_2010.pdf

we expect that customers in the CHCF-A areas would exhibit similar consumer behaviors.

4.3. The Communications Division Study of Small Rural Telephone Companies

CD conducted a study of small rural telephone companies that receive the CHCF-A support versus small carriers that do not. This was done using carrier submitted annual reports from 2003-2009.[47] The findings indicate major disparities among small ILECs that receive CHCF-A support versus those that do not and yet continue to serve similarly situated rural communities. A summary of the findings are provided below:

- Gross revenues per access line were over two times higher on average for the CHCF-A carriers than for the Non-CHCF-A carriers.
  - In 2009, the CHCF-A carriers earned four times more revenue per access line than the Non-CHCF-A carriers. Even with the CHCF-A fund support excluded, the CHCF-A carriers still earned gross revenues per access line that were two to three times more than their Non-CHCF-A counterparts.
- Net income per access line of the CHCF-A carriers was twice as much as their Non-CHCF-A counterparts on average.
  - In 2009, the CHCF-A carriers earned over eight times as much net income per access line as the Non-CHCF-A carriers.
- Total operating expenses per access line for the CHCF-A carriers were two and a half times higher than the Non-CHCF-A carriers on average.

[47] Carriers that did not receive funding from the CHCF-A were Happy Valley, Hornitos, Verizon West Coast, and Winterhaven.

- In 2009, the CHCF-A carriers spent four times as much as the Non-CHCF-A carriers. Significant expenditures for the CHCF-A carriers versus the Non-CHCF-A carriers 2008-2009 are as follows:
    - Five to six times more on corporate operating expenses;
    - Two to three times more on plant specific expenses; and
    - One and a half to two times more on Customer Operating expenses.
- On average, the CHCF-A carriers employed over two and a half times as much total plant in service (TPIS) per access line as the Non-CHCF-A carriers. In 2009, the CHCF-A carriers employed over eight times as much TPIS per access line as the Non-CHCF-A carriers. One factor contributing to this is that CHCF-A carriers have significantly more underground cable, while the Non-CHCF-A carriers have more aerial cable. Other significant capital investments by the CHCF-A carriers versus the Non-CHCF-A carriers are:
    - They are investing three times more on Land and Support; and
    - They are investing one and a half times more on Cable and Wire.

The study highlighted a clear distinction between the operating practices of carriers that receive CHCF-A support and those that do not. Carriers that received support were more profitable, yet far costlier to operate than those that did not. Additionally, carriers receiving funding from the CHCF-A, outspent the Non-CHCF-A carriers on capital infrastructure, most of which has applications beyond providing basic local telephone service and has the potential to provide unregulated services such as broadband and/or video services.

This study used multiple regression analysis to control for many independent variables such as topography/climate/location, customer density, carrier size, etc. to isolate the effect, if any, of receiving the CHCF-A funds. Analysis of various metrics confirmed that receipt of support from the CHCF-A has significant effects. For example, the marginal expense rate per access line, i.e. the cost of providing one additional access line, is nearly identical for similarly sized carriers who receive the CHCF-A subsidies and those that do not. However, carriers who receive CHCF-A support consistently spend substantially more per access line. We must question the causes of these differences and the implications for carrier funding through the CHCF-A.

At the very least, these findings suggest that a less efficient business model is being utilized by the small ILECs that receive support from the CHCF-A. Carriers receiving support funding from the CHCF-A program out spent Non-CHCF-A rural companies in renovation of facilities and in investment on new facilities. Yet, there is no indication that local telephone service is less readily available or less affordable for the customers who reside in territories serviced by the Non-CHCF-A carriers (also see Appendix I).

5. Preliminary Scoping Memo

It has been nearly 20 years since D.91-09-042 was issued outlining the procedures for the administration of the CHCF-A. The Commission recognizes that competition and technology have evolved over time and has determined that a review of CHCF-A fund is overdue. In this proceeding, the Commission seeks comments as well as updated information to comprehensively reassess the CHCF-A program.

As consumers embrace new services, their need for traditional landline telephone service may diminish. As a result, all telephone companies including the small ILECs, are experiencing a reduction in the number of landline telephone subscriptions, subsidized telephone lines included. However, contrary to expectations, the loss of these subsidized lines has not decreased the size of the CHCF-A and the subsidy per access line continues to rise. CHCF-A subsidized access line costs on average have risen from over two to four and half times as much as comparable CHCF-B lines (see Appendix J). Furthermore, the program has no evaluation or monitoring mechanism in place to verify that subsidy payments are used for intended purposes and whether they lead to prudent investments or operational efficiency.

These changes to the telecommunications landscape as well as D.10-02-016 require that we conduct a fully comprehensive examination of the CHCF-A program. We intend for this review to be forward-looking and adaptable to current and future regulatory and technological changes while still meeting the requirements of universal service and rate disparity minimization. This review should examine historical data with the aim of revising existing implementation rules governing the CHCF-A, assess its relevance in today's telecommunications environment, determine appropriate funding levels, and solicit comments from parties on proposed revisions to the rules governing the granting of support to small rural ILECs.

Interested parties should provide comments and specific proposals as set forth by the schedule below. To guide the parties' work on each topic, we pose several questions. These questions included here should not be interpreted as limitations but rather as starting points. We encourage all proposals to explicitly address consistency with statutory goals, necessity, feasibility, and cost effectiveness. Remedial proposals should also be included when identifying program deficiencies.

In this OIR, as a basis to meet these objectives, we request comment and proposals regarding the following issues.

5.1. CHCF-A Support Evaluation

One of the goals of the CHCF-A program is to maintain a fair and equitable local rate structure to promote universal service in high cost areas of California. Considering the current telecommunications landscape, we must determine if the program continues to be competitively and technologically neutral and whether the rate structure is fair and equitable. We must further evaluate to what extent support levels can be changed while still meeting the goals of this program.

In the past, the small ILEC territories were extremely isolated, and plain old telephone service was the only widely available service residents had for communication. Over the past few decades, population density has increased significantly across the state.[48] D.96-10-066 which created the CHCF-B anticipated that the need for subsidies may diminish over time due to competition and technological advancement.[49] This conclusion is equally applicable to the CHCF-A. New technologies such as wireless, satellite, and IP telephony have greatly increased consumers' communication options. However, these changes to California's population and telecommunications infrastructure have not resulted in cost savings for ratepayers or a reduction in the total CHCF-A fund draw.

CHCF-A carrier support shows significant increases from one year to the next. For example, the CHCF-A provided $21.9 million in carrier support in

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[48] U.S. Census Bureau, Population Division

[49] D.96-10-066 at 215.

2001. By 2005, the support had grown to $25.4 million, and by 2010, to $38 million (Appendix B).

In 2009, CHCF-A subsidized carriers reported approximately $45 million in local network service revenue and $26 million in long distance service revenue totaling $71 million. [50] Combined with the $37 million in CHCF-A subsidies with revenues from customers, California ratepayers paid over $108 million to CHCF-A carriers. That is almost $150 per month or over $1,700 per year per subsidized access line. To put that in perspective, the Commission could purchase each subsidized customer a satellite phone, pay for their service, and still produce a net savings to customers and ratepayers from $18 to $61 million per year.[51]

Given the current technological landscape and the abundance of competitive options, we question whether the CHCF-A program is still a necessary means to promote universal service. We seek comments as to whether we should terminate immediately, gradually discontinue, or alter provisions governing the CHCF-A program. Comments should address how such discontinuance or alteration may affect universal service goals.

5.2. Review of Program Implementation Rule

The CHCF-A program's implementation rules are outlined in the appendix to D.91-09-042. These rules include but are not limited to the filing of

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[50] Communications Division Study of Small Rural Telephone Companies.

[51] Figure based on Globalstar, Inc. GSP-1700 all you can talk voice plan, one year of unlimited service for $750 per line, totaling $47 million (as of 12/10). Ongoing cost figure based on Globstar, Inc. Liberty 6000 plan offering 12 months with 500 monthly minutes for $1,440 per line totaling $90 million.

Advice Letters by October 1st each year by the eligible small ILECs that submit a rate design and request CHCF-A support to offset the forecasted increase or decrease in revenues resulting from regulatory changes ordered by the Commission and FCC. The rules also establish the means test and the waterfall, which are triggered by an ILEC's submission of a GRC.

We solicit comments on whether the implementation rules adopted in D.91-09-042 are relevant given the current conditions that affect the small ILECs' service areas. Some conditions that are now changed from the time D.91-09-042 was adopted are increases in population, changes in costs triggered by technological developments and competition, as well as changes in small-ILEC company structures.

5.3. Determination of Carrier CHCF-A Funding Requirements

We ask whether there are ways of more accurately estimating the level of subsidy needed, if any, to promote the goal of universal service. The methodology developed to assess both estimated costs of basic service and subsidy levels needs to be repeatable and account for advances in technology, market developments, and demographic changes. The resulting process should be capable of accommodating modifications and/or policy changes from both the FCC and the California State Legislature which may impact this program. At the same time, any state support mechanism should not be obligated to make a carrier whole for any loss of federal support or any CHCF-A reform will be rendered moot.

We wish to explore whether the current fourteen small ILECs should continue to be classified as rate-of-return carriers and whether the current rate-of-return companies that have elected not to receive CHCF-A nor filed a GRC (per Ordering Paragraph 45 of D.94-09-065) should be required to file under the New Regulatory Framework (NRF) or Uniform Regulatory Framework (URF), thereby removing their eligibility for CHCF-A support.

In this proceeding, we will consider the following options to determine an appropriate carrier subsidy level. We encourage parties to explore these and other alternatives.

5.3.1. Implementing a Cap on the CHCF-A

In D.96-10-066, the Commission recognized that competition and technology would evolve over time and determined that a review of the CHCF-B should occur on a regular basis. The CHCF-A carriers are not subject to the same competitive pressure as the CHCF-B carriers. However, the Commission recognized in D.95-12-052 that the increase in the rate of productivity for telecommunications carriers should be equal to or greater than the rate of cost-inflation. Therefore, costs are expected to decrease, or at least remain fixed.

We believe that we should investigate why costs are not going down as technology advances and to consider appropriate actions to control the size of the CHCF-A while maintaining program goals. A cap on the CHCF-A subsidy may address this issue without a complex and costly investigation into the cause of the fund's increases. The responsibility for identifying and implementing cost efficiencies would be placed on the carriers. This solution has the advantage of being less intrusive in carrier operations while benefiting ratepayers.

We solicit comments on the implementation of a cap on the CHCF-A subsidy. Parties should comment on an initial cap amount, provide justification for that amount, and describe the expected effects on universal service. Comments should state the basis for the cap, whether it be number of access lines, capitalization, or another factor. If parties do not believe a cap is an appropriate solution then they should describe alternate means of controlling the size of the fund.

5.3.2. Basis for Urban Rate Caps

Under the CHCF-A implementation rules, the local exchange residential flat rates of the small ILECs should not exceed 150% of California urban rates. The existing residential flat rates in the small ILECs service areas range from $16.05 to $20.25.[52][53] Appendix G shows the existing rates of the fourteen small ILECs. With the deregulation of urban rates in California, the relationship between these rates and the rates of the small ILECs must be addressed.

Parties should state whether the 150% of urban rates cap is still reasonable in today's environment considering large carriers' urban rates are no longer subject to rate regulation in California. Parties should also comment on the elasticity of demand for telecommunications services in today's environment, and the reasonableness of using CD's affordability study as a proxy for service demand and various rates in the CHCF-A areas.

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[52] Carriers who receive CHCF-A support have rates set at $20.25 per month for basic telephone service. Carriers who do not receive CHCF-A support have rates from $16.05 to $16.85.

[53] D.0-02-016 Ordering paragraph 3: The use of the Pacific Bell Telephone Company dba AT&T California, Inc.'s basic rate as the required proxy for urban rates in applying the 150% guideline set forth in D.1-09-042 is hereby continued subject to the following restriction: The basic residential flat rate that a Small Local Exchange Carrier must charge to qualify for California High-Cost Fund A funding shall be fixed at the current level of $20.25 per month. This interim requirement shall continue in effect until the Commission adopts a decision in the California High-Cost Fund A rulemaking resolving pertinent reform issues, or otherwise modifies the restriction.

5.3.3. Standardizing Accepted Costs Among Carriers

When CD examined the small ILEC annual reports, it found there to be a wide variance in the reported costs for common elements. Revenues, expenses, and capital expenditures that were expected to be similar for common expense categories such as customer and corporate operations in fact varied widely. These findings call into question the overall efficiency with which the subsidized small ILECs operate when compared to similar carriers.

We wish to investigate the possibility of standardizing acceptable cost levels. If we could establish reasonable cost parameters by expense category, we could dispense with difficult and time consuming GRCs in favor of simple adjustments that could be made to CHCF-A support levels without requiring a full blown rate case.

5.3.4. Per Access Line Subsidy

Costs could be further standardized by administering the CHCF-A in a manner similar to the CHCF-B. The CHCF-B uses a Cost Proxy Model developed as part of the Commission's 1995 Universal Service proceeding I.95-01-021 and finalized in Implementing Rate Design D.96-10-066. This model uses internal and external carrier data to estimate the average cost to serve access lines within a Census Block Group in California.

This model was created for use by large incumbent ILECs, but we believe it is worth exploring the possibility of creating a similar model to suit the current CHCF-A eligible carriers. Use of such a model would partially or possibly fully obviate the need for GRCs.

The costs established by the model could be used in lieu of actual company expenses in order to determine funding for this specific carrier type.

This would further incentivize carriers to reduce costs in order to increase profitability.

CHCF-B carriers are paid the difference between established costs and a threshold. Using this method for the CHCF-A would greatly reduce the complexity of administration for carriers and Commission staff. In addition, the protocol for claims submission and payment is already in place further simplifying matters.

Parties should discuss how cost models can be used, as part of an effort to provide an access line subsidy to the CHCF-A eligible carriers. Parties should include a discussion of whether or not the Cost Proxy Model or something similar would be appropriate for the CHCF-A. Comments should state what modifications if any they believe would be necessary. Additionally we request comments on how to transition carriers from the current mechanism to a per access line subsidy. Parties should discuss whether an immediate change is appropriate or if changes should be phased in over time.

5.4. Monitoring Affiliate Transactions

Many of the small ILECs have affiliate companies that provide unregulated services, such as Internet and television, over their CHCF-A subsidized networks. Carriers are required to file affiliate transaction reports along with their annual reports, which document transactions between these entities.[54] CD conducted a brief review of affiliate transactions and has determined that the relationships between parent companies and affiliates are very complex, and not sufficiently transparent in the annual reports filed. From

[54] GO 66-C, Pub. Util. Code § 583.

this source, it cannot be determined whether affiliates are paying fair market rates for their use of the regulated networks.

We seek comments on the need to more closely monitor small ILEC affiliate transactions in light of the many new uses of their networks including the provision of unregulated services. Parties should state whether they believe closer monitoring is necessary, and if a modification to the annual reporting requirements is warranted. If parties believe that the small ILECs are not receiving fair market rates for use of their networks, they should provide potential solutions to remedy the situation.

5.5. Opening Small ILEC Territories to Competition

Decades ago, small ILECs were granted exclusive rights to do business in their franchised service territory. In 1995, competitors were granted full access to the four large ILECs' territory, and the right to apply to provide service in the small ILECs' territories.[55][56] However, the Commission has not yet authorized any wireline competition in small ILEC territories.

The Commission encourages competition wherever possible to reduce prices and foster innovation. At one time, economies of scale were such that competition in small ILEC territories was deemed unsustainable. However, given the current telecommunications landscape, we must revisit the Commission's policies on competition in small ILEC territories.

We solicit comments from parties on the effects of opening the small ILEC territories to wireline competition and consequences for universal service.

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[55] The four large ILECs are AT&T, Verizon, SureWest, and Frontier.

[56] D.95-07-054 opened California up to telecommunications competition.

We request comments from potential competitors identifying any barriers to entry into those markets, and what they believe the Commission could do to eliminate them.

6. Solicitation of Comments

Based upon the relevant scope of inquiry as set forth above, we envision the review of the CHCF-A program as illustrated in Appendix H. We therefore solicit comments on the following issues:[57]

A. CHCF-A Support Evaluation

1. Has the CHCF-A met its goal of promoting universal service while minimizing rate disparity?
2. If the CHCF-A has met its goal, should it be discontinued immediately or should it be phased out over time?
3. If the CHCF-A support should be phased out, should it be done in accordance with the current "waterfall" mechanism?
4. If the CHCF-A fund is discontinued or altered, is there a need for a monitoring mechanism to assure that universal service goals continue to be met?
5. If the CHCF-A has met its goals, should new goals be adopted based on changes in the needs of consumers, technological advancements, competition in the market, and California objectives?

B. Review of Program Implementation Rules

1. What implementation rules must be revised to account for proposed program changes?

[57] To the extent questions identified for comment in the preceding text are not explicitly set forth below, parties are still expected to address those questions in their filed comments.

2. Should new rules be adopted? If so, what rules, and why?
3. Should the current fourteen small ILECs continue to be classified as rate of return carriers?
4. Should the carriers who have elected not to receive CHCF-A support be reclassified as Non-CHCF-A eligible carriers, thus reducing the number of eligible carriers? How should they then be considered, for ratemaking purposes?

C. Implementing a Cap on the CHCF-A

1. Should the Commission implement a cap on the CHCF-A subsidy?
2. If a cap is implemented, how should the amount be determined?
3. What affects could a cap have on universal service?

D. Basis for Urban Rate Caps

1. Should AT&T's urban rate which is currently used as a basis for a small ILEC's rate design continue to be used going forward to determine basic service rates?
2. Should the small ILECs' rates be adjusted automatically in response to changes in AT&T's rates?
3. How should small ILECs' rates be determined if AT&T's rates are no longer regulated?
4. How should the small ILECs' basic residential rates be determined now that full pricing flexibility has been realized by the URF ILECs?
5. Should the Commission consider phasing-in the small ILECs' subsequent increases in basic rates over a defined time period to avoid rate shock?
6. Should the Commission consider granting current CHCF-A eligible small ILECs full pricing flexibility?

7. Should the Commission adopt a different mechanism for determining the CHCF-A basic residential service rate?

E. Standardizing Accepted Costs Among Carriers

1. Which carrier costs can be standardized for eligible carriers?
2. Should standard costs be established?
3. How often and by what means should costs be reviewed and/or adjusted?

F. Per Access Line Subsidy

1. Should the Commission establish a per access line subsidy for CHCF-A eligible carriers?
2. Should all small carriers be subject to the same per access line subsidy amount or should amounts be established on a per carrier basis?
3. Would the cost threshold model used for the CHCF-B be appropriate for the CHCF-A?
4. If a per access line subsidy is established, how should the Commission transition from rate of return regulation to a per access line subsidy?

G. Monitoring Affiliate Transactions

1. Should the rules for affiliate transactions be modified?
2. Should the Commission adopt new reporting requirements for affiliate transactions?
3. How should fair market rates for the use of regulated networks by affiliates be calculated?
4. Should affiliates' rates of return be considered when determining that of the regulated entity?

H. Opening Small ILEC Territories to Competition

1. Should wireline competition be allowed in small ILEC territories?

2. When evaluating the presence of competition should all communications technologies be considered?

I. Alternative Models to Consider

1. Should an Incentive-Benchmark Subsidy Model be considered in which carriers are rewarded for improving efficiency in operations, enhanced market penetration of universal service, and prudent investments?
2. Should an End-User-Direct Subsidy Model be considered in which the payment of a subsidy is directed to end users?
3. Should a Risk-Sharing Subsidy Model be considered in which, business risks are shared between shareholders and rate payers? For example, should any non-regulated revenues generated from the investment of the CHCF-A fund subsidy mechanism, like capital investment in infrastructure, be shared with the CHCF-A fund?
4. Should a Total Operations Model be considered in which, all communications services including landline telephone service, broadband, VoIP, etc. are included for ratemaking purposes?
5. Should the Commission consider purchasing services for rural customers from alternative providers to reduce costs?
6. What factors should the Commission consider to determine if an alternative provider is a suitable substitute?
7. What other subsidy mechanisms should the Commission consider in this review?

J. General Issues

1. How can the CHCF-A program administration be made more efficient?
2. Should we consolidate the CHCF-A with other public programs to efficiently capture the synergic potential of programs? If so, what programs should be included?
3. Should the entire small ILEC service territory remain eligible for high cost support? If not, what areas should be eligible for CHCF-A support?
4. Should the CHCF-A subsidy be expanded to cover other voice communication technologies such as wireless and VoIP?
5. What other issues should the Commission consider in this review?
6. What impacts will developments in the FCC USF proceeding have on the CHCF-A program?
7. Should the CHCF-A subsidy be de-linked from the federal subsidy?

7. Category of Proceeding

The Commission's Rules of Practice and Procedure require that an order instituting rulemaking preliminarily determine the category of the proceeding and the need for hearing.[58] As a preliminary matter, we determine that this proceeding is quasi-legislative. As provided in Rule 6(c) (2), any person who objects to the preliminary categorization of this rulemaking as "quasi-legislative" or to the preliminary hearing determination, shall file and serve its objections with its opening comments.

[58] Rule 6(c)(2).

8. Schedule

The preliminary schedule is set forth below. We delegate to the Assigned Commissioner and the ALJ the authority to set other dates in the proceeding or modify those below as necessary.

Day 1	Order Instituting Rulemaking issued
Day 16	Deadline for requests to be on service list
Day 61	Initial Comments filed and served
Day 91	Reply Comments filed and served

The determination on the need for further procedural measures, including discovery, technical workshops, and/or evidentiary hearings will be made in one or more rulings issued by the Assigned Commissioner. Any party who believes that an evidentiary hearing is required shall file a motion requesting such a hearing no later than ten business days after the filing of reply comments. Any such motion must identify and describe (i) the material issues of fact, (ii) the evidence the party proposes to introduce at the requested hearing, and (iii) the schedule for conducting the hearing. Any right that a party may otherwise have to an evidentiary hearing will be waived if the party does not submit a timely motion requesting an evidentiary hearing.

Following receipt of any such motions, the assigned Commissioner and ALJ shall determine the need for and extent of further procedural steps that are necessary to develop an adequate record to resolve this rulemaking, and shall issue rulings providing guidance to parties, as warranted.

This proceeding will conform to the statutory case management deadline for quasi-legislative matters set forth in Pub. Util. Code §1701.5.

9. Parties and Service List

The temporary service list for this proceeding shall be the combined lists from R.01-08-002 and A.99-09-044, the most recent proceedings addressing

CHCF-A issues. In addition, due to the far reaching effects of this proceeding, we will serve all remaining California telephone carriers.

Any person who wishes to become a party to this proceeding shall, within fifteen (15) days after the issuance of this order, send a request to the Commission's Process Office via electronic mail (process_office@cpuc.ca.gov) or by postal mail (Process Office, CPUC, 505 Van Ness Avenue, San Francisco, California 94102) to be placed on the official service list in this proceeding. Parties who only wish to monitor the proceedings, but not participate as an active party, shall indicate that they be added to the "Information Only" section of the service list. The service list will be posted on the Commission's website: www.cpuc.ca.gov prior to the time comments are filed pursuant to Ordering Paragraph 8.

Any person or party interested in participating in this rulemaking but who is unfamiliar with the Commission's procedures should contact the Commission's Public Advisor in Los Angeles at (213) 649-4782 or in San Francisco at (415) 703-7074, (866) 836-7875 (TTY-toll free) or (415) 703-5282 (TTY) or send an e-mail to public.advisor@cpuc.ca.gov.

The Commission has adopted rules for the electronic service of documents related to its proceedings, Commission Rule 2.3.1, available on our website at http://www.cpuc.ca.gov/PUBLISHED/RULES_PRAC_PROC/44887.htm. All parties shall comply with the requirements of this rule.

10. Ex parte Communications

Per Rule 7(d) of the Commission's Rules of Practice and Procedure, ex parte communications are allowed without restriction or reporting requirement in any quasi-legislative proceeding. Therefore, there are no such restrictions or reporting requirements applied to this proceeding.

Therefore, **IT IS ORDERED** that:

1. A rulemaking is instituted for the purpose of reviewing the California High Cost Fund-A Program.

2. The issues to be considered in this proceeding are defined in the Preliminary Scoping Memo as a specific need to take any warranted remedial action regarding the subsidy mechanism for the California High Cost Fund–A program and a need to thoroughly review the program in light of market and technological developments.

3. The Executive Director shall cause this Order Instituting Rulemaking to be served on all telecommunications carriers, California High Cost Fund-A Administrative Committee, and parties on the service list of Rulemaking 01-08-002 and Application 99-09-044.

4. Any person who wishes to become a party to this proceeding shall, within fifteen (15) days after the issuance of this order, send a request to the Commission's Process Office via electronic mail (process_office@cpuc.ca.gov) or by postal mail (Process Office, CPUC, 505 Van Ness Avenue, San Francisco, California 94102) to be placed on the official service list in this proceeding. Parties who only wish to monitor the proceedings, but not participate as an active party shall indicate that they be added to the "Information Only" section of the service list. The service list will be posted on the Commission's website: www.cpuc.ca.gov prior to the time comments are filed pursuant to Ordering Paragraph 8.

5. All parties shall abide by the Commission's new electronic service rules contained in Rule 2.3.1 of the Commission's Rules of Practice and Procedure.

6. We preliminarily determine the category of this rulemaking to be "quasi-legislative" and preliminarily determine that hearings are unnecessary.

Parties objecting to these determinations shall include their objections in their opening comments.

7. Any party who believes that an evidentiary hearing is required shall file a motion requesting such a hearing no later than 10 business days after reply comments are due. Any such motion must identify and describe (i) the material issues of fact, (ii) the evidence the party proposes to introduce at the requested hearing, and (iii) the schedule for conducting the hearing. Any right that a party may otherwise have to an evidentiary hearing will be waived if the party does not submit a timely motion requesting an evidentiary hearing.

8. Respondents shall include the 14 small Incumbent Local Exchange Carriers.

9. Respondents shall, and other parties may, file opening comments on the issues identified in this rulemaking according to the schedule set forth in this order.

10. The assigned Commissioner and Administrative Law Judge will set the schedule for this proceeding by subsequent rulings, as warranted, to develop the record and to bring this rulemaking to a conclusion.

This order is effective today.

Dated ____________________________, at San Francisco, California.

Appendix A
Wireless Subscribership Facts

Facts	Jun-10	Jun-05	Jun-00	Jun-95	Jun-90	Jun-85	Jan-85
Wireless Subscriber Connections (Millions)	292.8	194.4	97	28.1	4.4	0.2	0.09
Wireless Penetration (% of total U.S. Population)	93	66	34	11	n/a	n/a	n/a
Wireless-Only Households (% of U.S. Households)	0.245	0.077	n/a	n/a	n/a	n/a	n/a
Average Local Monthly Bill (June Survey)	$47.47	$49.49	$45.15	$52.45	$83.94	n/a	n/a
Minutes of Use (annualized)	2.26T	1.26T	194.95B	31.5B	n/a	n/a	n/a
Annualized SMS Message Total	1.81T	57.2B	n/a	n/a	n/a	n/a	n/a

Note: **B=Billion, T=Trillion**

Wireless Substitution: Early Release of Estimates from the National Health Interview Survey, July - December 2009, National Center for Health Statistics, May 2010.

Source:

1. http://www.ctia.org/media/industry_info/index.cfm/AID/10323

2. CTIA Survey Mid Year 2010

3. http://www.ctia.org/advocacy/research/index.cfm/AID/10323

(END OF APPENDIX A)

Appendix B

CHCF-A Support to Small ILECs (In Dollars)
1998 – 2010

(END OF APPENDIX B)

Appendix C

Small ILECs' Revenue Requirement Requests to the CHCF-A (In Dollars)*

*As made by each carrier before the means test and waterfall provision are applied.

(END OF APPENDIX C)

Appendix D

Number of Access Lines Per Small ILEC

	Average Lines			
	2007	**2008**	**2009**	**2010**
Calaveras	4,360	4,243	4,047	3,896
Cal-Ore	2,585	2,510	2,286	2,139
Citizens GS	14,692	13,895	n/a	n/a
Citizens T	6,621	6,488	n/a	n/a
Ducor	1,325	1,264	1,197	1,157
Foresthill	2,946	2,946	2,887	2,985
Global Valley	15,322	11,470	n/a	n/a
Happy Valley	3,440	3,219	3,163	3,056
Hornitos	671	642	598	592
Kerman	6,833	6,833	6,407	5,926
Pinnacles	270	262	257	253
Ponderosa	9,508	8,981	8,727	8,543
Sierra	22,892	22,548	21,797	21,093
Siskiyou	4,589	4,471	4,219	4,237
Verizon WC	13,511	13,511	15,995	10,213
Volcano	11,475	10,792	10,483	11,595
Winterhaven	1,346	1,246	1,297	1,228
Total	122,386	115,321	83,360	76,913

(END OF APPENDIX D)

Appendix E

History of CHCF-A Surcharge Rate

Effective	Surcharge Rate
12/1/2010	0.000%
5/1/2010	0.110%
1/1/2010	0.130%
12/1/2009	0.130%
6/1/2008	0.130%
1/1/2008	0.130%
4/1/2007	0.210%
8/1/2006	0.210%
1/1/2006	0.210%
4/1/2005	0.150%
1/1/2005	0.170%
8/1/2004	0.170%
2/1/2004	0.170%
1/1/2004	0.170%
9/1/2003	0.210%
7/1/2003	0.210%
5/1/2003	0.210%
3/1/2003	0.360%
1/1/2003	0.360%
10/1/2002	0.360%
7/1/2002	0.360%
1/1/2002	0.300%
12/1/2001	0.200%
11/1/2001	0.200%
9/1/2001	0.200%
7/1/2001	0.200%
1/1/2001	0.000%
6/1/2000	0.000%
1/1/2000	0.000%
1/1/1999	0.000%
8/1/1998	0.000%
1/1/1998	0.000%
2/1/1997	0.000%
1/1/1996	0.270%
1/1/1995	0.500%

(END OF APPENDIX E)

Appendix F

Communications Expenditures per Household per Month in Dollars

Source: Number of households from the Census Bureau's Current Population Survey. Expenditure data from the Bureau Of Economic Analysis, National Economic Accounts, Table 2.4.5U. Personal Consumption Expenditures by Type of Product. See http://www.bea.gov/national/nipaweb/nipa_underlying/SelectTable.asp last visited June 8, 2010. In Trends in

Year	Landline Telephone Services	Cellular Telephone Services	Internet Access Services	Total Telephone and Internet Access
1984	$40	$0	$0	$40
1990	$51	$2	$0	$53
1995	$62	$9	$1	$72
2000	$77	$26	$13	$116
2005	$56	$51	$22	$128
2009	$54	$67	$31	$152

Telephony September 2010, FCC Data extracted from Table 3.4.

(END OF APPENDIX F)

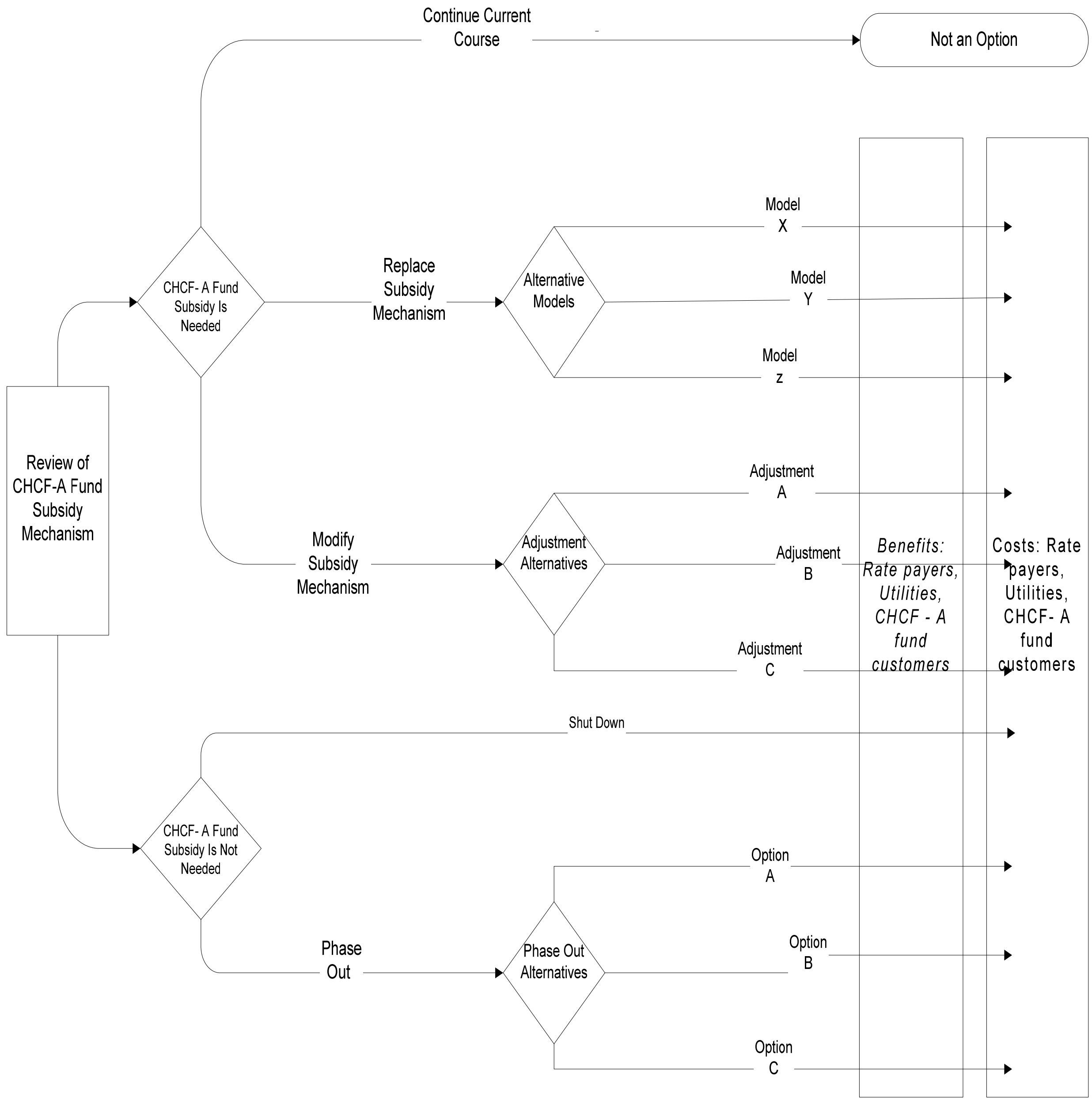
Appendix G

CHCF-A Small ILECs' Basic Residential Service Rates
As of February 2010

Carrier	**Basic Residential Rate**
Calaveras Telephone Company	$20.25
Cal-Ore Telephone Company	$20.25
Ducor Telephone Company	$20.25
Foresthill Telephone Company	$16.05
Happy Valley Telephone Company	$16.85
Hornitos Telephone Company	$16.05
Kerman Telephone Company	$19.40
Pinnacles Telephone Company	$20.25
Ponderosa Telephone Company	$20.25
Sierra Telephone Company	$16.85
Siskiyou Telephone Company	$16.85
Verizon West Coast Incorporated	$16.85
Volcano Telephone Company	$16.85
Winterhaven Telephone Company	$17.50

(END OF APPENDIX G)

Appendix H
Proceeding Flow Chart



(END OF APPENDIX H)

Appendix I

Small ILECs' Key Financial Statistics
CHCF-A Subsidized vs. Unsubsidized

Table 1: Access Lines

	2003	2004	2005	2006	2007	2008	2009
Access Lines							
Total Access Lines	124,718	125,114	124,095	123,312	122,386	115,321	83,360
Subsidized Lines	81,127	78,517	64,746	64,559	66,783	64,850	62,307

Table 2: CHCF-A

	2003	2004	2005	2006	2007	2008	2009
CHCF-A							
Total CHCF-A Subsidy*	$31,870,002	$30,395,320	$25,446,077	$28,096,729	$31,393,619	$29,992,396	$36,747,758
Average CHCF-A Subsidy Per Line*	$393	$387	$393	$435	$470	$462	$590

Table 3: Revenue

	2003	2004	2005	2006	2007	2008	2009
Revenue							
Average Revenue Per Line (A Fund Carriers)	$1,673	$1,707	$1,840	$1,904	$1,983	$2,022	$2,183
Average Revenue Per Line (Non A Fund Carriers)	$874	$887	$870	$857	$808	$827	$573

Table 4: Expense

	2003	2004	2005	2006	2007	2008	2009
Expense							
Average Expense Per Line (A Fund Carriers)	$1,196	$1,227	$1,384	$1,429	$1,510	$1,536	$1,639
Average Expense Per Line (Non A Fund Carriers)	$530	$603	$672	$567	$512	$548	$401
Average Plant Specific Exp Per Line (A Fund)	$313	$373	$447	$496	$486	$509	$489
Avg Plant Specific Exp Per Line (Non A Fund)	$96	$113	$126	$136	$127	$159	$201
Average Customer Exp Per Line (A Fund Carriers)	$152	$135	$137	$141	$150	$156	$172
Avg Customer Exp Per Line (Non A Fund Carriers)	$89	$114	$115	$90	$83	$98	$89
Average Corporate Exp Per Line (A Fund Carriers)	$413	$414	$473	$523	$565	$601	$677
Avg Corporate Exp Per Line (Non A Fund Carriers)	$105	$171	$214	$152	$116	$102	$142

Table 5: Income

	2003	2004	2005	2006	2007	2008	2009
Income							
Average Net Income Per Line (A Fund Carriers)	$254	$249	$229	$408	$324	$229	$241
Avg Net Inc Less Subsidy Per Line (A Fund Carriers)	-$139	-$138	-$164	-$27	-$146	-$234	-$348
Average Net Income Per Line (Non A Fund Carriers)	$181	$104	$103	$204	$92	$151	$29

Table 6: Plant

	2003	2004	2005	2006	2007	2008	2009
Plant							
Average TPIS** Per Line (A Fund Carriers)	$2,009	$2,288	$2,423	$2,420	$2,707	$2,982	$3,187
Average TPIS** Per Line (Non A Fund Carriers)	$993	$1,009	$1,071	$913	$964	$1,168	$387
Avg Land&Support Per Line (A Fund Carriers)	$1,247	$1,371	$1,486	$1,525	$1,506	$1,628	$1,779
Avg Land&Support Per Line (Non A Fund Carriers)	$472	$465	$489	$464	$499	$556	$679
Avg CO*** Switching Per Line (A Fund Carriers)	$1,139	$1,131	$1,159	$1,222	$1,220	$1,181	$1,182
Avg CO*** Switching Per Line (Non A Fund Carriers)	$756	$944	$917	$777	$803	$878	$975
Average Transmission Per Line (A Fund Carriers)	$1,076	$1,234	$1,502	$1,545	$1,554	$1,660	$1,808
Average Transmission Per Line (Non A Fund Carriers)	$818	$896	$855	$792	$914	$1,020	$1,218
Average Cable&Wire Per Line (A Fund Carriers)	$3,052	$3,397	$3,915	$4,238	$4,734	$5,048	$5,678
Average Cable&Wire Per Line (Non A Fund Carriers)	$2,520	$2,503	$2,332	$2,543	$2,559	$2,796	$3,363
Avg Aerial Cable Per Line (A Fund Carriers)	$120	$136	$148	$154	$200	$202	$164
Avg Aerial Cable Per Line (Non A Fund Carriers)	$361	$311	$283	$306	$378	$337	$361
Average Miles of Cable Per AL (A Fund Carriers)	0.15	0.16	0.18	0.19	0.18	0.19	0.20
Average Miles Cable Per AL (Non A Fund Carriers)	0.11	0.11	0.10	0.10	0.11	0.12	0.18
Avg Cable&Wire Plant Per Mi Cable (A Fund)	$23,694	$24,603	$25,831	$26,919	$30,328	$30,839	$33,259
Avg Cable&Wire Plant Per Mi Cable (Non A Fund)	$24,558	$26,021	$25,192	$26,420	$25,083	$25,774	$12,918

** Total Plant in Service
*** Central Office

Table 7: Rate of Return

	2003	2004	2005	2006	2007	2008	2009
Rate of Return							
Average ROR **** (A Fund Carriers)	13%	11%	9%	17%	12%	8%	8%
Average ROR **** (Non A Fund Carriers)	18%	10%	10%	22%	10%	13%	7%
Average ROR **** (A Fund Carriers) Without Subsidy	-3%	-5%	-5%	1%	-4%	-7%	-10%

**** Total Company Rate of Return (regulated and unregulated)

(END OF APPENDIX I)

Appendix J

Comparison of High Cost Funds A and B Monthly Funding

	Average Lines			
	2007	2008	2009	2010
Total (CHCF-B)	3,281,363	1,165,014	374,760	288,000
Total (CHCF-A)	122,386	115,321	83,360	76,913
	Annual Funding			
Total (CHCF-B)	$383,082,069	$196,048,742	$68,455,395	$31,947,787
Total (CHCF-A)	$31,393,619	$29,992,396	$36,784,801	$37,977,459
	Annual Funding / Line			
Total (CHCF-B)	$116.74	$168.28	$182.66	$110.93
Total (CHCF-A)	$257	$260	$441	$494
	Monthly Funding / Line			
	2007	2008	2009	2010
Total (CHCF-B)	$9.73	$14.02	$15.22	$9.24
Total (CHCF-A)	$21	$22	$37	$41

(END OF APPENDIX J)