
**SENATE COMMITTEE ON ENERGY, UTILITIES AND
COMMUNICATIONS**

**Senator Steven Bradford, Chair
2023 - 2024 Regular**

Bill No: SB 754 **Hearing Date:** 4/10/2023
Author: Alvarado-Gil
Version: 3/21/2023 Amended
Urgency: No **Fiscal:** Yes
Consultant: Sarah Smith

SUBJECT: Communications: California High-Cost Fund-A Administrative Committee Fund program

DIGEST: This bill clarifies rate-making requirements for small independent telephone corporations to prohibit the California Public Utilities Commission (CPUC) from incorporating broadband revenues in calculations for telephone corporation rates.

ANALYSIS:

Existing law:

- 1) Establishes the California High Cost Fund – A (CHCF-A) program to provide support to small independent telephone companies in rural, high-cost areas of the state to ensure residents’ access to affordable telecommunications services in these communities. (Public Utilities Code §275)
- 2) Authorizes the CPUC to administer a surcharge to fund the CHCF-A, and specifies that CHCF-A moneys appropriated to the CPUC may only be used for the administration of the CHCF-A program. (Public Utilities Code §275)
- 3) Establishes various definitions for the administration of the CHCF-A, including, but not limited to, the following definitions:
 - a) “Rate base” means the value of a telephone corporation’s plant and equipment that is reasonably necessary to provide regulated voice services and access to advanced services, and upon which the telephone corporation is entitled to a fair opportunity to earn a reasonable rate of return.
 - b) “Rate design” means the mix of end user rates, high-cost support, and other revenue sources that are targeted to provide a fair opportunity to meet the revenue requirement of the telephone corporation.
 - c) “Rate-of-return regulation” means a regulatory structure whereby the commission establishes a telephone corporation’s revenue requirement, and

then fashions a rate design to provide the company a fair opportunity to meet the revenue requirement.

- d) “Revenue requirement” means the amount that is necessary for a telephone corporation to recover its reasonable expenses and tax liabilities and earn a reasonable rate of return. (Public Utilities Code §275.6)
- 4) Existing law requires the CPUC to regulate the rates of telephone corporations receiving CHCF-A subsidies, and it requires the CPUC to use subsidies from the CHCF-A fund to cover those reasonable costs that these small independent telephone corporations cannot recover through rates. (Public Utilities Code §275.6)
- 5) Existing law requires the CPUC to take certain steps when engaging in rate cases for CHCF-A companies, including, but not limited to, promote customer access to broadband services and ensure that subsidies from the CHCF-A are not so excessive that they become a burden on all telecommunications ratepayers. (Public Utilities Code §275.6)
- 6) Requires CHCF-A companies to provide the CPUC with information about revenues it receives from its broadband service upon request. Existing law requires the CPUC to treat this information as confidential. (Public Utilities Code §276.5)
- 7) Sunsets the CHCF-A on January 1, 2028. (Public Utilities Code §276.5)

This bill:

- 1) Clarifies that the CHCF-A program is intended to ensure that telephone rates in high-cost, rural service territories remain reasonable and sufficient incentives exist for small independent telephone corporations to invest in broadband-capable facilities. This bill clarifies that providing these incentives does not confer regulatory or ratemaking authority over internet service providers or internet access services.
- 2) Modifies several existing definitions to specify that rate design does not include revenue from internet access services, other nonregulated services, or interstate services regulated under the authority of the Federal Communications Commission (FCC).
- 3) Requires the CPUC to ensure that each small telephone corporation’s rate design equals its revenue requirement and sufficient to meet its revenue requirement.

- 4) Clarifies that providing the CPUC with broadband revenue information does not change the scope of the CPUC's jurisdiction over internet service providers or internet access services.
- 5) Requires the CPUC to adjust each small independent telephone corporation's rate design by February 1, 2024, to remove any broadband or internet access revenues and implement corresponding increases to the CHCF-A program for each small independent telephone corporation to ensure that its rate design equals its revenue requirement.

Background

CHCF-A. The CHCF-A is one of several programs that comprise California's Universal Service Programs, which are aimed at ensuring that all Californians have access to affordable, high quality telecommunications services. Under existing law, the CHCF-A program provides rate support to small independent telephone corporations. These small independent telephone corporations are "Carriers of Last Resort" that are required to provide telephone service to individuals when no other carrier is willing to provide service. The rate assistance provided by the CHCF-A program is intended to ensure that residents in rural communities can access telecommunications services at rates comparable to those for similar services in urban areas. Rural telecommunications rates can significantly exceed urban rates due to higher infrastructure costs and a lack of economies of scale. While the amount needed to cover costs for CHCF-A company expenses is determined through rate cases at the CPUC, claims submitted by the small independent telephone corporations for CHCF-A subsidies have remained relatively stable and have not risen with the rate of inflation.

Bill seeks to exclude broadband revenues from telephone corporation rate case calculations. Generally, existing law establishes the rate case process to ensure that regulated utilities receive sufficient revenues to provide safe, affordable, quality service for customers. Existing law also generally requires rate design to ensure that regulated utilities earn a sufficient profit margin. This bill makes various changes to existing law governing CPUC rate cases for telephone corporations receiving support from the CHCF-A. These changes are intended to clarify that the CPUC may not use broadband revenues to calculate the revenue requirements of the small independent telephone corporations. While the CHCF-A program was originally established to support rural telephone corporation rates, these small independent telephone corporation have since developed broadband services. Existing federal rules distinguish telephone corporation services from broadband services. As a result, the small independent telephone corporations

operate broadband services through affiliated companies. This bill prohibits the CPUC from including the revenues of these broadband affiliate companies when determining the revenues of the telephone corporations and the amount of money needed to profitably operate the telephone corporation.

How did we get here? In 2011, the FCC took steps to expand its support for broadband deployment by shifting federal telecommunications infrastructure support from telephone to broadband infrastructure. To remain eligible for these subsidies, carriers needed to demonstrate that they were making progress towards meeting broadband deployment goals. At the time, stakeholders were concerned that if carriers were unable to upgrade their facilities to meet the Connect America Fund minimum speeds, the state would lose the opportunity to draw down federal subsidies and telephone corporations would more heavily rely on high cost fund support, including the CHCF-A. The CPUC opened a proceeding (R.11-11-007) to address concerns about the small independent telephone corporations' potential federal subsidy loss and greater reliance on state rate support. At the time, stakeholders expressed concern that the CPUC would not permit the small independent telephone corporations to use their funding, which include CHCF-A monies, to deploy broadband infrastructure because internet service is not rate-regulated. To better enable these small telephone corporations to invest in broadband infrastructure the Legislature passed SB 379 (Fuller, Chapter 729, Statutes of 2012), which aligned state CHCF-A statutes with the federal shift towards broadband subsidies and enabled the CPUC to obtain information about the revenues generated by broadband affiliates of the small independent telephone corporations.

The CPUC has kept its CHCF-A rulemaking open since 2011 and periodically adopted decisions making substantial changes to the program. In 2021, the CPUC adopted a decision (D.21-04-005) that requires the imputation of all broadband revenues obtained by the small independent telephone corporations within their California high cost areas. This decision treats revenues from the broadband affiliates as monies that can be used to subsidize revenue needs of the telephone corporation. In turn, it reduces these telephone corporations' draw from the CHCF-A fund in proportion to the profits the broadband affiliate earns. Under this imputation scheme, it is unlikely that in-state broadband investments by these affiliates will generate significant profits within high cost areas of the state. As the CPUC has reduced these companies' subsidies from the CHCF-A program through broadband imputation, the CPUC has also increased ratepayer costs for customers of these small independent telephone corporations. In many cases, the rates approved by the CPUC exceed the rates proposed by the companies themselves.

The CPUC and the small independent telephone corporations are still engaged in litigation regarding the imputation decision; however, the most recent court decision affirmed the CPUC's decision. This decision substantially relied on inferring legislative intent; however, the decision also noted that the statutes were broad and legislative direction was ambiguous. The court reasoned that the Legislature would not have provided the CPUC with the broadband affiliates' revenue data if the Legislature had not intended for the CPUC to use that data to reduce subsidies from the CHCF-A program. While SB 379 made it clear that the Legislature expressly directed the CPUC to ensure that CHCF-A needs did not burden ratepayers, the bill makes no reference to using broadband subsidies to reduce telephone corporations' ability to obtain CHCF-A subsidies.

This bill would clarify that the CPUC may not impute broadband revenues in telephone corporation rate cases. This bill also requires the CPUC to continue to limit excessive draws from the CHCF-A program that would burden ratepayers; however, it also requires the CPUC to ensure that CHCF-A companies receive sufficient revenue support to keep telephone rates affordable. While this bill would likely require the CPUC to revise its imputation decision, a new proceeding would not be necessary since the existing CHCF-A rulemaking proceeding remains open.

Does broadband imputation align with state broadband deployment goals? The small independent telephone corporations remain the only telecommunications providers in the state that are limited on their ability to earn profits from broadband affiliates. Since the CPUC adopted a decision to impute these affiliates' revenues within high cost areas of the state, California has taken steps to issue substantial grants to deploy broadband infrastructure in unserved parts of the state. These grants are largely funded through taxpayer revenues – not ratepayer funds. While some affordability requirements have been set for these grants, these grant programs do not cap broadband revenues. In some cases, the CPUC has explicitly prioritized the deployment of broadband funding to locations where networks would be more economically sustainable. It is unclear how a broadband affiliate of a small independent telephone corporation could make a business case for obtaining these grants to deploy broadband in their high cost areas given that their profits would be imputed in subsequent rate cases.

To regulate, or not regulate: that is the (increasingly ambiguous) question. While this bill prohibits the CPUC from including broadband revenues in revenue requirements for certain small telephone corporation rate cases, this bill does not foreclose the CPUC from regulating internet service rates to the extent that the CPUC gains the authority to do so. The Obama FCC adopted rules reclassifying internet service as a more strictly regulated common carrier under Title II of the federal *Communications Act*. Subsequently, the Trump FCC adopted rules

reverting internet service to an information service under Title I of the *Communications Act*. While the Trump FCC's rules limited the treatment of internet service as a strictly regulated utility, subsequent court decisions determined that the Trump FCC overstepped its legal authority in automatically pre-empting states from adopting their own net neutrality rules. While court decisions have indicated that states may regulate internet services more actively in areas where the FCC has declined to adopt rules, these court decisions have not specifically addressed the question of state-level rate regulation of internet services. In the event that policies are clarified to facilitate state-level ratemaking over internet services, this bill would not prohibit the CPUC from doing so. Instead, it requires the CPUC to distinguish between the fully rate-regulated telephone corporation and the less-regulated broadband affiliate during telephone corporation rate cases, and it limits the CPUC from co-mingling the revenues of the telephone corporation and broadband affiliate when determining the revenue needs of the telephone corporation.

Need for amendments. As currently written, this bill could be interpreted to require the CPUC to increase the size of the CHCF-A program by February 1, 2024, as part of redesigning rates pursuant to this bill. This implication does not appear to be the author's intent. *As a result, the author and committee may wish to amend this bill to clarify that the amount companies receive from the CHCF-A may be adjusted to reflect the removal of broadband revenues, but the CHCF-A program should not be expanded.*

Prior/Related Legislation

SB 857 (Hueso, Chapter Chapter 706, Statutes of 2022) extended the sunset for the CHCF-A and B programs from January 1, 2023, to January 1, 2028.

AB 1257 (Patterson, 2021) would have required the CPUC to hold at least one day of facilitated mediation before proceeding with a small independent telephone corporation's rate case, and the bill would have required the CPUC to meet and confer with proceeding parties at least one before filing a motion to make a good faith effort to informally resolve the motion's concerns. The bill was held in the Senate Appropriations Committee.

SB 603 (Borgeas, 2019) would have allowed small independent telephone corporations to use either an application or advice letter process to initiate a rate case. The bill was held in the Assembly Appropriations Committee.

AB 1959 (Wood, Chapter 256, Statutes of 2018) extended the sunset for the CHCF-A and B programs from January 1, 2019, to January 1, 2023.

SB 1122 (Canella, 2016) would have required the CPUC to issue a final decision for a small independent telephone corporation rate case no later than 390 days after the corporation files its application or advice letter initiating the case. The bill also would have authorized the small independent telephone corporations to file tariffs implementing interim rates if CPUC failed to issue a final decision by the 390th day. The bill died in the Assembly.

AB 1693 (Perea, 2014) would have required the CPUC to issue a final decision for a small independent telephone corporation rate case no later than 390 days after the corporation files its application or advice letter initiating the case. The bill also would have established a process for implementing an interim rate proposed by the corporations if the CPUC failed to meet the deadline. The bill was vetoed.

SB 379 (Fuller, Chapter 729, Statutes of 2012), allowed CHCF-A subsidies for broadband-enabled infrastructure and allowed the CPUC to obtain information about the revenues generated by broadband affiliates of the small independent telephone corporations.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: Yes

SUPPORT:

California Communications Association, Co-sponsor
California's Independent Telecommunications Companies, Co-sponsor
Almond Alliance
Association of California Healthcare Districts
Ducor Union Elementary School District
Economic Development Corporation of Mariposa County
Kerman Chamber of Commerce
Mariposa County Board of Supervisors
Mariposa County Chamber of Commerce
Mariposa County Office of Education
Mariposa County Sheriff's Office of Emergency Services
Mariposa County Unified School District
Oakhurst Area Chamber of Commerce
Rotary Club of Mariposa Yosemite
USTelecom - the Broadband Association

OPPOSITION:

The Utility Reform Network

ARGUMENTS IN SUPPORT: According to the author:

SB 754 reverses a CPUC decision that is contrary to the Legislature's goal of connecting rural Californians to high-speed broadband. The CPUC is cutting funding that the small rural telephone companies need for upgrading their networks with fiber in some of the most rural areas of the state. In practical terms, this funding is critical for the rural communities they serve to have access to high-speed broadband, which allows for democratic engagement, social mobility, and economic equality and growth.

ARGUMENTS IN OPPOSITION: The Utility Reform Network (TURN) opposes this bill because it argues that removing broadband affiliate revenues from the independent telephone corporation's revenue calculations would lead these telephone corporations to draw on CHCF-A monies to keep telephone rates affordable in high cost areas of the state. In opposition, TURN states: "TURN opposes SB 754 because it would result in excessive CHCF-A support to companies at the expense of consumers who pay the CHCF-A subsidy."

-- END --