

**PUBLIC UTILITIES COMMISSION**505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298**FILED**10-30-06
03:51 PM

October 30, 2006

Agenda ID #6123
Ratesetting

TO PARTIES OF RECORD IN APPLICATION 05-03-005

This is the proposed decision of Administrative Law Judge (ALJ) Bushey. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. The Commission may act then, or it may postpone action until later.

When the Commission acts on the proposed decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the proposed decision as provided in Article 14 of the Commission's **Rules of Practice and Procedure** (Rules), accessible on the Commission's website at www.cpuc.ca.gov. Pursuant to Rule 14.3, opening comments shall not exceed 15 pages.

Comments must be filed either electronically pursuant to Resolution ALJ-188 or with the Commission's Docket Office. Comments should be served on parties to this proceeding in accordance with Rules 1.9 and 1.10. Electronic copies of comments should be sent to ALJ Bushey at mab@cpuc.ca.gov. All parties must serve hard copies on the ALJ and the Assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service. The current service list for this proceeding is available on the Commission's website at www.cpuc.ca.gov.

/s/ ANGELA K. MINKINAngela K. Minkin, Chief
Administrative Law Judge

ANG:tcg

Attachment

Decision **PROPOSED DECISION OF ALJ BUSHEY** (Mailed 10/30/2006)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SBC California (U 1001 C) for a Surcharge and a Balancing Account to Recover Undergrounding Costs in the City of San Diego.

Application 05-03-005
(Filed March 3, 2005)

OPINION AUTHORIZING MODIFIED SURCHARGE TO RECOVER COSTS OF UNDERGROUNDING AERIAL TELEPHONE LINES

I. Summary

In this decision, we grant the request of Pacific Bell Telephone Company, doing business as SBC California (SBC)¹ for a surcharge to recover the costs of undergrounding its aerial telephone lines in San Diego. We modify SBC's proposed rate design for the surcharge from a fixed amount to a percentage of all intrastate revenue.

II. Background

In January 2001, the City of San Diego (City) adopted its Underground Utilities Procedural Ordinance to provide for the expedited undergrounding of overhead utility wires within the city limits. The City's goal is to underground all currently overhead utility lines in 20 years. To accomplish this goal, the City must quadruple the current rate at which utility lines are undergrounded.

¹ Now known as AT&T California, Inc.

This Commission has adopted comprehensive, statewide rules that govern when and where a utility may remove overhead lines and replace them with underground service, and whether such costs will be recovered through rates. These rules are set forth in Tariff Rule 32 for SBC and Tariff Rule 20 for San Diego Gas and Electric Company (SDG&E). To accommodate the City's ordinance, SDG&E sought Commission authorization to deviate from Tariff Rule 20. In Resolution E-3788, the Commission granted both SDG&E and SBC permission to deviate from their respective tariffs and comply with the City's ordinance.

To finance SDG&E's portion of the undergrounding project, the City and SDG&E entered into an agreement whereby the franchise fee SDG&E pays to the City would increase from 1.9% of gross revenues to 5.78%. Ninety percent of the increased funds would be used by the City to pay for the undergrounding. The Commission also authorized SDG&E to increase the City's franchise fee surcharge to all City customers to reflect the increased fee, and directed SBC to file an application to seek permission to recover its increased undergrounding costs from City customers.

On March 3, 2005, SBC filed this application to approve a surcharge and balancing account to track and recover its costs for the City undergrounding project. SBC estimated that the total cost of the San Diego undergrounding project would be \$125 million and that the project would extend over 17 years. SBC requested an initial surcharge of \$0.94 per customer line per month, to be adjusted annually via the balancing account.

On April 7, 2005, the Utility Consumers' Action Network (UCAN) protested the application, arguing that undergrounding costs are before the Commission in the undergrounding rulemaking (Rulemaking 00-01-005). UCAN

also found SBC's cost estimates to be "shockingly high" and suggested that the proposed cost recovery might violate the New Regulatory Framework under which the Commission regulates SBC's rates.

On April 18, 2005, the Division of Ratepayer Advocates (DRA) filed a motion requesting permission to late-file its protest to this application, which was granted on May 3, 2005. DRA also challenged the requested relief as violating New Regulatory Framework principles.

Telscape Communications, Inc. (Telscape), XO Communications, Inc., MPower Communications Corp., and the California Association of Competitive Telephone Companies also protested the application.

DRA and a coalition of the competitive carriers filed motions to dismiss the application, contending that it violated both federal law and the New Regulatory Framework under which this Commission regulates SBC. SBC and the City opposed the motions. On May 24, 2005, the assigned Administrative Law Judge (ALJ) convened a prehearing conference and set a procedural schedule to resolve the motions to dismiss. The Commission denied the motions to dismiss in Decision (D.) 05-10-028.

The assigned ALJ convened a second prehearing conference on December 5, 2005, and set a procedural schedule to address the merits of the application. After completing discovery, the parties distributed written direct testimony. Evidentiary hearings were held on May 15 and 16, 2006. The parties filed opening briefs on June 16, 2006, and the proceeding was submitted for Commission consideration with the filing of closing briefs on July 7, 2006.

III. Positions of the Parties

A. SBC

SBC did not prepare a detailed cost forecast based on its own costs but instead relied on the historical relationship of its undergrounding costs to SDG&E's costs.² SBC's costs have historically been about 23% of SDG&E's, so SBC applied the 23% factor to SDG&E's cost forecast for 2007 through 2023 to obtain the annual forecasted cost for SBC.

SBC proposed a flat fee rate design for its surcharge to recover the cost of the San Diego undergrounding project. SBC calculated the fixed amount surcharge per customer line by dividing the total annual forecasted cost by the average number of access lines in service in San Diego, 657,000 lines. (This amount includes all lines served by SBC and other local exchange carriers.) The result is the annual amount which must be recovered from each access line. The monthly surcharge per line is determined by dividing the annual total by 12, which SBC calculated to be \$0.77 for 2007 and \$1.51 for 2008. The remaining years showed a forecasted surcharge of about \$0.90 per month per line.

SBC proposed to apply this surcharge to all customer access lines it serves directly, as well as all lines SBC provides to competitive local exchange carriers for resale to San Diego end users.

SBC did not exempt from the surcharge low-income customers eligible for discounted local exchange service in the Lifeline program. SBC stated it had no information on the number of low-income program participants taking service

² Aerial telephone and electricity lines are often undergrounded simultaneously so SBC and SDG&E have a long history of joint undergrounding projects.

from the competitive local exchange carriers, and thus no practical way to reflect any such customer exemptions in calculating the surcharge. Because it could not exempt competitive local exchange carriers' low-income customers, SBC did not propose to exempt its low-income customers from the surcharge.

The City supported SBC's proposal.

B. UCAN

UCAN contended that SBC's proposal was anti-consumer and anti-competitive. UCAN stated that SBC's fixed monthly fee proposal was regressive because it would disproportionately impact low- and fixed-income customers, who often have few competitive choices. In contrast, the benefits of undergrounding will accrue disproportionately to homeowners, as property values rise due to improved appearance. UCAN further contended that SBC would be able to cross-subsidize its competitive service offerings by recovering the cost of network enhancements through the undergrounding surcharge on regulated services.

C. Telscape

Telscape opposed SBC's proposal to assess the undergrounding surcharge on Lifeline customers. Telscape explained that SBC's surcharge would amount to a 20% increase in Lifeline rates for local residential service, with no offsetting benefits. Telscape recommended that Lifeline customers be exempt from the surcharge and that the City should make up the shortfall in undergrounding costs.

Telscape also asked that the Commission modify SBC's surcharge by excluding costs where SBC is installing additional capacity, apportion costs to the unused capacity, allocate costs based on use of the system, require pro-rating

of the surcharge for partial months, and allow for chargeback of any uncollectible surcharge revenues.

D. XO Communications Services, Inc.

XO also opposed SBC's application and argued that "the Commission's jurisdiction and authority are being eroded and undermined by the City's attempt to force [SBC] to act as its collection agent to recover the costs of the undergrounding program."

Specifically, XO contended that the Commission has set up a statewide program for undergrounding, balancing the costs and benefits. Granting SBC's requested surcharge would encourage other cities to by-pass the Commission's program, adopt similar ordinances, and expect the Commission to order surcharges to recover the costs. Furthermore, XO continued, Commission-approved Lifeline rates will be increased by approximately 30% due to the undergrounding surcharge, in derogation of the Commission's determination of the appropriate rate for low-income customers. XO concluded that SBC's proposal was also anticompetitive because certain of SBC's customers that take service pursuant to contracts, rather than tariffs, will not be assessed the surcharge.

XO also stated that SBC was already recovering the costs of undergrounding through its existing rates, as approved by this Commission in the New Regulatory Framework, and in the setting of prices for unbundled network elements, which are purchased by competitive local carriers, such as XO. The surcharge represents a double-counting of these costs.

Finally, the detailed auditing necessary to ensure that SBC does not improperly charge unrelated costs to the surcharge balancing account is impractical due to expense and oversight needed.

E. Division of Ratepayer Advocates

DRA opposed the surcharge as being inconsistent with the New Regulatory Framework which set SBC's prices to include the cost of undergrounding. DRA also opposed the notion of a fixed or per line surcharge as being unprecedented at this Commission, and advocated that Lifeline program participants be exempt from the surcharge.

If the Commission were to adopt a surcharge, DRA recommended that it be proportionally assessed to all SBC customers based on total purchases from SBC and all its affiliates. DRA's proposed to allocate costs between Commission-jurisdictional services and other services, e.g., based on total billed amounts in San Diego. The surcharge on jurisdictional services would be set to recover a share of total undergrounding costs calculated by the proportion of jurisdictional sales in San Diego to total sales. SBC would have discretion to recover the remaining costs, i.e., the nonjurisdictional fraction, from its nonjurisdictional customers. DRA pointed to the Commission's Reimbursement Fee, which applies a surcharge of 0.11% to all jurisdictional revenue, as an example of the surcharges on which its proposal was modeled.

Finally, DRA objected to SBC's cost forecasts as being "far higher than publicly available data of actual expenditures." DRA supported a "monitoring and audit program equivalent to that applied to SDG&E."

IV. Discussion

The applicant, SBC, bears the burden of proving that its proposed surcharge is "justified." Pursuant to Pub. Util. Code § 454(a), prior to implementing the surcharge, SBC must make a "showing before the Commission," and, based on that showing, the Commission must find that the surcharge is "justified."

As discussed in detail below, we find SBC's showing on the forecasted costs to be scant; we therefore adopt limitations and oversight modeled on those applied to SDG&E. We find SBC's showing failed to justify its proposed rate design. Consistent with our precedent for other similar public policy surcharges, we will require that SBC assess the surcharge as a percentage of intrastate revenue. Prior to considering the specifics of SBC's proposal, however, we address the issue of our statewide plan for undergrounding utility lines and future applications similar to SBC's.

A. The Commission's Undergrounding Program

As discussed above, the Commission has adopted a long-standing program to determine an undergrounding program, in concert with the affected electric and telephone utilities. In Rulemaking 00-01-005, the Commission acted on Legislative directive (AB 1149) by studying ways to amend, revise, and improve rules for the conversion of existing overhead electric and communications lines to underground. The legislation required that the Commission study ways to: 1) eliminate barriers to undergrounding and to prevent uneven patches of overhead facilities; 2) enhance public safety; 3) improve reliability; and 4) provide more flexibility and control to local governments. The Commission issued an interim decision in that proceeding, D.01-12-009, which expanded the use of the existing program, and set several contentious issues for a subsequent Phase 2. That Phase has not yet been completed.

The parties in this proceeding raised policy issues regarding the wisdom of the Commission allowing its general ratemaking authority to be used by the City as a mechanism to collect the costs of undergrounding utility lines.

Undergrounding utility lines is extremely expensive. With the proposed surcharge, San Diego residents will be paying an extra \$4 per month in utility charges (\$3 to SDG&E and \$1 to SBC), on top of any other price increases. The Commission has historically shouldered the burden of balancing the costs of undergrounding with the benefits in adopting uniform statewide policies. With today's decision and Resolution E-3788, this Commission has allowed the City to effectively short-circuit the long-standing plan.

Extraordinary and unique events led to today's decision. Most significantly, the SDG&E franchise fee increase has been in place for some time and actual work on this project has commenced. On balance, the totality of the circumstances supports going forward with this surcharge despite its inconsistency with the statewide plan. We direct our staff to advise any utilities seeking such measures, either as surcharges or increases in franchise fees, that the statewide plan controls utility undergrounding.

B. Cost Forecasts

SBC provided no forecasts based on its actual costs in support of its proposed surcharge. Instead, SBC witness Kieren derived SBC's cost forecast from SDG&E's forecast of its cost to underground its facilities in the same areas. SDG&E estimated \$28.3 million for 2007, \$51.8 million for 2008, and \$31 million for each year thereafter until 2023. SBC multiplied SDG&E's annual amount by 0.23, which is the historical ratio of SBC's to SDG&E's costs. SBC's annual amount was then divided by 657,000 lines, which is the current average number of access lines in service in San Diego. Finally, the result was divided by 12 to arrive at a forecasted monthly per line surcharge.

SBC proposed to use a balancing account to track actual labor and expense costs associated with undergrounding and to adjust the surcharge up or down as

needed. The surcharge would also be adjusted to reflect changes in the number of access lines in San Diego. The collected surcharge funds would be held in an interest bearing account.

In short, SBC's surcharge proposal, which is contemplated to collect over \$125 million, is derived from three numbers obtained from SDG&E – cost estimates for 2007, 2008, and \$31 million for each year thereafter. Other than elementary mathematical manipulation, SBC added nothing to SDG&E's forecasts.

SBC, however, is not in any way bound to the cost forecasts. SBC proposed to recover its actual costs over the 17-year project by recording those costs in a balancing account and then setting the surcharge to recover that amount. After setting the initial surcharge, which will be subject to true up to actuals, the cost forecasts will be irrelevant.

Accordingly, the key elements of SBC's proposal are the recording of actual costs and the balancing account to ensure full recovery. These two elements work together to allow SBC a direct path from recorded costs to customers' bills.

SBC proposes to send an annual report to the Director of the Commission's Telecommunications Division to "allow the Commission to track and validate the cost associated with the project and the correctness of the surcharge amount."

XO witness Knowles was skeptical that SBC's promised annual reports would be sufficient to allow the type of detailed auditing required for this \$125 million, 17-year project. Knowles testified that SBC could be tempted to load up the undergrounding surcharge account "with all manner of oversight, management, supervision, systems development and general costs." Annual reports with very little detail will not be sufficient to thwart this temptation.

We agree. SBC's proposed virtually no oversight of costs that might be recorded in the balancing account, and the surcharge will enable SBC to recover the recorded amounts directly from customers. Detailed auditing and oversight, however, would require a commitment of significant Commission and SBC resources.

As an alternative, we find that the historic ratio of SBC's and SDG&E's undergrounding costs provides a convenient point of reference for evaluating future costs. To the extent SBC's future costs exceed this historic ratio, we will impose enhanced oversight obligations on SBC.

If, as XO fears, SBC allocates unrelated costs to the San Diego undergrounding project, then SBC's costs would be expected to exceed 23% of SDG&E's. Such an increase would be a signal to the Commission, and the parties, that greater scrutiny of the cost allocations is required. On the other hand, if the historical ratio remains stable in the future, then the Commission would have some evidence that SBC is not allocating unrelated costs to the San Diego undergrounding program.

Therefore, to the extent SBC's costs do not exceed 23% of SDG&E's costs in any calendar year, SBC will be required to submit a semi-annual report to the Telecommunications Division Director showing the status of the project, items recorded in the balancing account, and surcharge calculations. Supporting detail should also be available. SBC's semi-annual reports shall be filed contemporaneously with SDG&E's similar reports to the Energy Division. Each report shall show the ratio between SBC's and SDG&E's costs. The surcharge shall be recalculated annually via advice letter filing, with supporting workpapers.

Heightened review will be required should SBC's undergrounding costs exceed 23% of SDG&E's costs for the areas included in a particular semi-annual report. A semi-annual report with such a showing should be submitted to the Executive Director, who shall investigate the cause. Unless the amount by which the 23% has been exceeded is: 1) immaterial or 2) readily explained by easily verified facts, the Executive Director shall authorize an audit of SBC's balancing account.³ The audit will be funded by SBC, with the total costs of the audit not to exceed 1% of total costs proposed to be recorded in the balancing account that year. Until the cost allocation issues have been resolved, no changes will be made in the surcharge.

Finally, in D.05-10-028, we directed the assigned Commissioner and ALJ to manage this proceeding to ensure that a full factual and legal record was created for our consideration on the issue of whether the undergrounding costs were included in SBC's New Regulatory Framework and network element revenue requirements. Allowing the same costs to be used as a basis for the surcharge would result in double-counting.

SBC's witness explained that SBC's undergrounding projects in San Diego which occur pursuant to SBC's tariff Rule 32 program will be segregated from the undergrounding projects required by the City's ordinance. SBC witness McDaniel testified that SBC will underground lines in San Diego simultaneously under both the tariff rule 32 program and as required by the City's ordinance.

³ Such an audit may be performed by Commission auditors or outside vendors as deemed appropriate by the Director of the Telecommunications Division.

Because the tariff rule 32 program requires detailed cost accounting, SBC will be required to separately record and track the costs associated with each program.

This explanation, coupled with the auditing requirement imposed above, is sufficient to resolve the issue from our earlier decision.

In conclusion, we will authorize SBC to establish a San Diego Utilities Underground Utilities Procedural Ordinance balancing account, and to record costs associated with undergrounding aerial telephone lines pursuant to that ordinance in the account.

C. Applicability of the Surcharge

SBC proposed to apply the fixed surcharge to each line issued to customers that subscribe to business and residential telephone service.⁴ The parties took issue with SBC's proposal to exclude certain contracts from the surcharge unless the contracts allow for such charges. The parties also objected to SBC's proposal to include two types of customers - Lifeline and Wholesale Customers for two-wire voice grade UNE loops. Lifeline customers are participants in the Commission's program that provides basic telephone service at reduced rates to low-income customers. Wholesale customers that purchase two-wire voice grade UNE loops use that wholesale service to support their own local telephone service which they offer to end-user customers.

As analyzed below, our precedent requires that public policy surcharges, such as this, be applied to the widest possible customer base and that SBC has not presented a persuasive justification for excluding certain contracts from the

⁴ 1FR, 1MR, 1MB, Centrex, ISDN Basic, Business Lines and Trunks, California 900, Direct Connection, FEX Lines, FPS Lines, PSP/COPT, ISDN PRI, PBX (Retail and Resale classes), Residence (Flat, Measured, ADL, and Lifeline) and SDS56.

surcharge. Similarly, end users served by wholesale customers also should be subject to the surcharge. Based on our precedent, we do, however, exclude Lifeline service from the surcharge.

XO witness Knowles objected to SBC's plan to impose the proposed surcharge on lines served pursuant to certain⁵ contracts "to the extent applicable contracts allow it." Knowles explained that SBC has not identified the number of customers or lines that might be included in this surcharge exemption, nor stated a rationale for treating these customers differently from similarly situated customers. Knowles concluded that excluding certain wholesale customers but not others, such as XO, constituted anticompetitive discrimination.

The Public Utilities Code requires that SBC justify its proposal to exclude customers from the surcharge. SBC's evidence on this point is limited to an assertion that customers will not be included where the "contract does not allow the surcharge to be applied." SBC has not provided for the record copies of any such contractual language, estimates of the numbers of lines to which this exemption would apply, nor any calculation of amount by which the surcharge will be increased to reflect these exemptions.

Our long-standing goal is to apply public policy surcharges to "the widest possible customer base." See, e.g., *Re Alternative Regulatory Frameworks for Local Exchange Carriers*, 56 CPUC 2d 117, 266 (D.94-09-065). SBC has proposed to exclude an unidentified share of the base from such a surcharge with only conclusory statements unsupported by record evidence. SBC has not provided

⁵ SBC's rebuttal testimony suggests that customers taking service pursuant to Local Wholesale Complete, Individual Case Basis, Express, and Government contracts may be exempted from the surcharge if contract "does not allow the surcharge to be applied."

sufficient justification for its decision to exclude any such pre-existing contracts from the surcharge, nor has SBC explained how it will prevent this class of exempted service from expanding. Therefore, we deny this portion of SBC's proposal and order SBC to impose the San Diego undergrounding surcharge on all intrastate services provided in San Diego, whether provided pursuant to contract or tariff.

UCAN and DRA oppose SBC's proposal to apply its surcharge to all residential service lines participating in the Lifeline program. UCAN and DRA contend that this proposal is regressive and that SBC's rationale is not persuasive.

SBC concedes that it could easily exempt its own Lifeline customers from the surcharge. However, no means has been proposed or developed to exempt the Lifeline customers of the competitive local carriers from the surcharge. SBC concludes that, therefore, all Lifeline customers must be included in the surcharge.

We disagree. As discussed in more detail below, the Commission has created a number of public purpose programs which are funded by a surcharge on intrastate revenue. Lifeline service⁶ is exempt from these surcharges. See *Re Alternative Regulatory Frameworks for Local Exchange Carriers*, 56 CPUC 2d 117, 266 (D.94-09-065). The same methodology and process used for assessing these surcharges, and exempting Lifeline service, should be applied to the San Diego undergrounding surcharge. In this way, all Lifeline service, whether provided by SBC or a competitive local carrier, will be exempt from the surcharge.

⁶ Any additional services purchased by the Lifeline customer are subject to the surcharge.

A similar result occurs with regard to Telscape's and XO's continuing objection to applying the surcharge to services provided by competitive local exchange carriers. These carriers calculate and collect the surcharges listed below from their customers. This same process should be applied for the San Diego undergrounding surcharge.

D. Rate Design of Surcharge

SBC stated that a flat rate surcharge more appropriately reflects the costs and benefits of undergrounding aerial telephone lines. The costs are driven by the number of wire pairs that must be placed underground. Each pair costs the same to underground regardless of the amount of telephone services provided over the line. The benefits of undergrounding, which the City describes as primarily aesthetic, are shared equally by each resident, again regardless of the amount of telephone services provided.

As set out above, UCAN and DRA objected to the fixed amount surcharge as being regressive and unprecedented by this Commission.

SBC did not challenge the "regressive" characterization, but in its reply brief did cite to two Commission-approved fixed amount surcharges. The cited surcharges – one cent per year for number portability surcharge and 25 cents per month for payphones – are both *de minimus* amounts adopted as fixed surcharges primarily for administrative convenience, not after a thorough analysis of the Commission's policy against regressive surcharges. See *Re Competitive for Local Exchange Service*, 83 CPUC 2d 408 (D.98-12-044) (adopting one cent per year number portability surcharge because "the actual computed surcharge is less than one cent per line and fractions of a cent cannot be collected from customers."), and *Re Statewide Expansion of Public Policy Pay Telephones*, 83 CPUC 2d 41, 50-52 (D.98-11-029) (noting that pursuant to a settlement agreement,

payphone providers pay the surcharge, rather than the Commission adopting a “broad based public service funding method.”)

The surcharge SBC proposes requires just such a broad based public service funding method. The Commission’s typical rate design for this type of surcharge is a percentage of intrastate revenue.

The Commission has adopted surcharges on intrastate revenues for the following public policy programs:

Program	Surcharge	Purpose
Lifeline	1.29%	Provide reduced rate service to low-income customers
California Relay Service and Communications Devices Fund	0.27%	Provide equipment and relay service to deaf and disabled customers
CPUC User Fee	0.11%	Provide funding for Commission operations
High Cost Fund A	0.21%	Provide subsidy for geographically expensive areas (small carriers)
High Cost Fund B	2.00%	Provide subsidy for geographically expensive areas (large carriers)
California Teleconnect Fund	0.13%	Provide discounted telecommunications service to schools, libraries, and medical clinics

Each competitive and incumbent local exchange carrier in California must assess these surcharges on all intrastate revenues, and remit the collected funds to the Commission. See, e.g., *Application of Transcend Multimedia, LLC for a Certificate of Public Convenience and Necessity to Operate as a Provider of Resold Local Exchange Telecommunications Service Within the State of California*, D.06-07-009 (July 20, 2006).

SBC has provided us no persuasive rationale for deviating from this long-standing surcharge rate design. Similarly, DRA has not provided compelling rationale to allocate to services beyond our jurisdiction a fraction of the amount to be collected. Accordingly, we will modify the rate design of SBC's surcharge proposal to a percentage of intrastate revenue.

In conclusion, we will authorize SBC to assess the City of San Diego Surcharge for Underground Conversion Costs on the intrastate revenues from all San Diego customers, with the exception of Lifeline service. The surcharge shall be calculated annually, and SBC shall file an advice letter setting forth its calculations with supporting documentation.

V. Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and Maribeth A. Bushey is the assigned ALJ in this proceeding.

VI. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311 and Rule 14.2(a) of the Rules of Practice and Procedure. Comments were filed on _____.

Findings of Fact

1. SBC did not prepare its own cost forecasts for the San Diego undergrounding project but rather relied on the historical ratio of its and SDG&E's undergrounding costs, 23%, and SDG&E's costs forecasts as the basis for its application.
2. The Commission has adopted a long-standing, detailed, and comprehensive program for undergrounding utility lines. Extraordinary and unique events support the deviations from that program set forth in this decision and Resolution E-3788.

3. SBC provided scant cost justification for its proposed surcharge, and key elements of the proposal are the recording of actual costs and balancing account recovery to ensure SBC full recovery of all recorded costs.

4. SBC proposed virtually no oversight on its cost records.

5. The historic undergrounding cost ratio between SBC and SDG&E provides a reasonable standard against which to initially assess the validity of SBC's costs. To the extent SBC's costs exceed 23% of SDG&E's, enhanced oversight is required.

6. SBC provided no analysis of the number of lines or customers that might be exempt from the proposed surcharge pursuant to contractual terms.

7. Long-standing Commission precedent exempts Lifeline service from public policy surcharges.

8. Competitive local carriers calculate and collect numerous public policy surcharges.

9. The Commission's typical rate design for public policy surcharges is a percentage of intrastate revenue.

Conclusions of Law

1. SBC bears the burden of proving that its proposed surcharge is justified.

2. SBC did not justify its proposal to exclude from the surcharge customers that take service pursuant to Local Wholesale Complete, Individual Case Basis, Express, and Government contracts. The City of San Diego Surcharge for Underground Conversion Costs should be modified to apply to all City customers, excluding Lifeline service.

3. So long as SBC's costs do not exceed 23% of SDG&E's costs for particular areas, SBC should be required to submit a semi-annual report to the Telecommunications Division Director showing the status of the project, items

recorded in the balancing account, and surcharge calculations. Supporting detail should also be available as required. SBC's semi-annual reports should be filed contemporaneously with SDG&E's similar reports to the Energy Division. Each report shall show the fractional relationship between SBC's and SDG&E's costs. The surcharge shall be recalculated annually via advice letter filing, with supporting workpapers.

4. If SBC's San Diego undergrounding costs exceed 23% of SDG&E's costs in a particular semi-annual report, the Director of the Telecommunications Division shall investigate the cause. Unless the amount by which the 23% has been exceeded is: 1) immaterial or 2) readily explained by easily verified facts, the Director of the Telecommunications Division shall conduct an audit of SBC's balancing account either using Commission staff or outside vendors. The audit will be funded by SBC, with the total costs of the audit not to exceed 1% of total costs proposed to be recorded in the balancing account that year. Until the cost allocation issues have been resolved, no changes will be made in the surcharge.

5. SBC has not justified its proposed flat fee rate design. The City of San Diego Surcharge for Underground Conversion Costs should be modified to use a percentage of intrastate revenue rather than a flat fee.

6. SBC has not justified its proposal to subject Lifeline service to the City of San Diego Surcharge for Underground Conversion Costs. SBC's proposed surcharge should be modified to exclude Lifeline service from the surcharge.

7. As modified, SBC's proposed City of San Diego Surcharge for Underground Conversion Costs should be adopted.

8. This decision should be effective immediately.

ORDER

IT IS ORDERED that:

1. The application of Pacific Bell Telephone Company, known as SBC California (SBC) when this application was filed but now known as AT&T California, Inc., for a balancing account for costs associated with undergrounding aerial telephone facilities in San Diego pursuant to the City of San Diego Underground Utilities Procedural Ordinance and the San Diego Surcharge for Underground Conversion Costs (Surcharge) for the assessment of those costs to San Diego customers, is granted subject to the limitations set forth herein.

2. All local telephone customers in San Diego, including SBC customers that take service pursuant to Local Wholesale Complete, Individual Case Basis, Express, and Government contracts, shall be subject to the Surcharge. Local telephone customers that receive service from competitive local exchange carriers are also subject to the Surcharge. Lifeline service from any provider is exempt from the Surcharge, but any other intrastate services provided to the Lifeline customer is subject to the Surcharge.

3. SBC shall submit a semi-annual report to the Director of the Telecommunications Division showing the status of the undergrounding project, items recorded in the balancing account, and Surcharge calculations. Supporting detail must also be provided as required. SBC's semi-annual reports should be filed contemporaneously with San Diego Gas & Electric's (SDG&E) similar reports to the Energy Division. Each SBC report shall show the fractional relationship between SBC's and SDG&E's costs for the lines included in the report.

4. The Surcharge shall be assessed as a percentage of intrastate revenue and separately stated on each customer bill. The Surcharge shall be recalculated

annually via advice letter filing, with supporting workpapers, and shall be timed to coincide with one of the semi-annual report filings.

5. If SBC's San Diego undergrounding costs exceed 23% of SDG&E's costs in a particular semi-annual report, the Executive Director shall investigate the cause. Unless the amount by which the 23% has been exceeded is: 1) immaterial or 2) readily explained by easily verified facts, the Executive Director shall conduct an audit of SBC's balancing account either using Commission staff or outside vendors. The audit will be funded by SBC, with the total costs of the audit not to exceed 1% of total costs proposed to be recorded in the balancing account that year. Until the undergrounding cost allocation issues have been resolved, no changes will be made in the surcharge.

This order is effective today.

Dated _____, at San Francisco, California.

INFORMATION REGARDING SERVICE

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Dated October 30, 2006, at San Francisco, California.

/s/ TERESITA C. GALLARDO

Teresita C. Gallardo

***** SERVICE LIST *****

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***** APPEARANCES *****

David J. Miller
Attorney At Law
AT&T CALIFORNIA
525 MARKET STREET
SAN FRANCISCO CA 94105
(415) 778-1393
davidjmiller@att.com
For: AT&T

Mary M. Adu
Legal Division
RM. 4107
505 VAN NESS AVE
San Francisco CA 94102 3298
(415) 703-1952
mma@cpuc.ca.gov

Sarah De Young
CALIFORNIA ASSOCIATION OF COMPETITIVE
50 CALIFORNIA STREET, SUITE 1500
SAN FRANCISCO CA 94111
(925) 465-4396
deyoung@caltel.org
For: CALTEL

Glenn Semow
LESLA LETHONEN
CALIFORNIA CABLE & TELECOMM. ASSOC.
360 22ND STREET, STE. 750
OAKLAND CA 94612
(510) 628-8043
grs@calcable.org
For: California Cable and Telecommunications Assoc.

John Clark
Attorney At Law
GOODIN MACBRIDE SQUERI RITCHIE & DAY LLP
505 SANSOME STREET, 9TH FLOOR
SAN FRANCISCO CA 94111
(415) 765-8443
jclark@gmsr.com
For: Telscape Communications, Inc.

Earl Nicholas Selby
Attorney At Law
LAW OFFICES OF EARL NICHOLAS SELBY
418 FLORENCE STREET
PALO ALTO CA 94301
(650) 323-0990
ens@loens.com
For: XO Communications Services, Inc.

David Discher
Attorney At Law
PACIFIC BELL TELEPHONE COMPANY
525 MARKET STREET, RM. 2027
SAN FRANCISCO CA 94105
(415) 778-1464
david.discher@att.com
For: SBC

Thomas Zeleny
Attorney At Law
SAN DIEGO CITY ATTORNEYS OFFICE
1200 THIRD AVENUE, SUITE 1100
SAN DIEGO CA 92101
(619) 533-5800
tzeleny@sandiego.gov
For: City of San Diego

Lori Ortenstone
Attorney At Law
SBC
ROOM 1300
101 W. BROADWAY
SAN DIEGO CA 92101
(619) 237-3329
lori.ortenstone@att.com
For: SBC

Pamela B. Baterina
Associate Director-Regulatory
SBC CALIFORNIA
525 MARKET ST., 19/F - 13
SAN FRANCISCO CA 94105
For: SBC California

Michael Shames
Attorney At Law
UTILITY CONSUMERS' ACTION NETWORK
3100 FIFTH AVENUE, SUITE B
SAN DIEGO CA 92103
(619) 696-6966
mshames@ucan.org
For: UCAN

***** STATE EMPLOYEE *****

Maribeth A. Bushey
Administrative Law Judge Division
RM. 5018
505 VAN NESS AVE
San Francisco CA 94102 3298
(415) 703-3362
mab@cpuc.ca.gov

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Laurence Chaset
Legal Division
RM. 5131
505 VAN NESS AVE
San Francisco CA 94102 3298
(415) 355-5595
lau@cpuc.ca.gov

William Johnston
Division of Ratepayer Advocates
RM. 4101
505 VAN NESS AVE
San Francisco CA 94102 3298
(415) 703-2256
wej@cpuc.ca.gov

***** INFORMATION ONLY *****

Noel D. Allan
LABRADOR WORLD, INC.
1183 VAN NUYS STREET
SAN DIEGO CA 92109
(858) 488-7882

Sara Steck Myers
Attorney At Law
LAW OFFICES OF SARA STECK MYERS
122 - 28TH AVENUE
SAN FRANCISCO CA 94121
(415) 387-1904
ssmyers@att.net

Bob Meijer
9052 GERALDINE PLACE
SAN DIEGO CA 92123
(619) 602-7250
rmeijer@sprynet.com

Marilyn H. Ash
MPOWER COMMUNICATIONS CORP.
175 SULLYS TRAIL, SUITE 300
PITTSFORD NY 14534
(585) 218-8729
mash@mpowercom.com
For: MPOWER COMMUNICATIONS CORP.

Margaret Tobias
Attorney At Law
TOBIAS LAW OFFICE
460 PENNSYLVANIA AVE
SAN FRANCISCO CA 94107
(415) 641-7833
info@tobiaslo.com

Jesus Roman
Asst. General Counsel
VERIZON
MAILCODE CA501LB
112 LAKEVIEW CANYON RD.
THOUSAND OAKS CA 91362
(805) 372-6233
jesus.g.roman@verizon.com

Jacque Lopez
VERIZON CALIFORNIA INC.
CA501LB
112 LAKEVIEW CANYON ROAD
THOUSAND OAKS CA 91362-3811
(805) 372-6664
jacque.lopez@verizon.com

Rex Knowles
Regional Vice President
XO COMMUNICATIONS SERVICES, INC.
111 EAST BROADWAY, SUITE 1000
SALT LAKE CITY UT 84111
(801) 983-1504
rex.knowles@xo.com

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