

BEFORE THE PUBLIC UTILITIES COMMISSION OF STATE OF CALIFORNIA

Order Instituting Investigation on the Commission's own motion into the alleged failure of TracFone Wireless, Inc. (U-4321-C) to collect and remit public purpose program surcharges and user fees on revenue from its sale of intrastate telephone service to California consumers, in violation of the laws, rules and regulations of this State; Order to Show Cause why Respondent should not immediately be ordered to pay all such outstanding sums plus interest, and be subject to penalties for such violations.

**FILED**  
**PUBLIC UTILITIES COMMISSION**  
**DECEMBER 17, 2009**  
**SAN FRANCISCO OFFICE**  
**L09-12-016**

**ORDER INSTITUTING INVESTIGATION**  
**INTO THE OPERATIONS OF TRACFONE WIRELESS, INC.**

**I. SUMMARY**

By this Order, the Commission institutes an Investigation into the failure of TracFone Wireless, Inc. (TracFone) to pay public purpose surcharges and user fees on its intrastate telephone revenue. The Commission orders TracFone to show cause why it should not immediately be ordered to pay all such outstanding sums, and be subject to possible additional remedies and penalties for violation of California statutes and Commission rules which require collection and remittance of public purpose surcharges and user fees.

**II. STAFF INVESTIGATION & FACTUAL ALLEGATIONS**

TracFone provides cellular or wireless telecommunication services -- bundled with wireless handsets -- to customers in California at market-based

rates, and has apparently done so since 1999.<sup>1</sup> TracFone resells minutes and network connectivity which it purchases on a wholesale basis from facilities-based carriers.

Customers prepay for their wireless service through TracFone. TracFone has its proprietary and copyrighted “software included in [the] telephone handsets” it sells to customers in California,<sup>2</sup> software that is used to manage and control the handsets and the purchase and sale of minutes of wireless service through the handset.<sup>3</sup>

TracFone’s agreement with Verizon Wireless, for instance, requires TracFone “to own, operate and maintain at all times during this Agreement the technology platform (‘Platform’) that supports and monitors the TracFone Handset.”<sup>4</sup> Its agreement with AT&T provides, similarly, that TracFone “must provide and maintain all Mobile Radio Unit equipment and ensure that it is technically and operationally compatible with the CMRS systems [of AT&T],”<sup>5</sup> and its agreement with T-Mobile refers to the “equipment,

<sup>1</sup> See accompanying Staff Report at 6 (TracFone payment of user fees from 1999-2004). As described in more detail in the accompanying Staff Report, the Wireless Registration Identification number used by TracFone was originally granted to a company named Topp Telecomm, Inc., in 1997. *Id.* at 2.

<sup>2</sup> TracFone’s October 13, 2009 Opening Comments on Proposed Resolution T-17235, at 8, fn. 7.

<sup>3</sup> *TracFone Wireless, Inc. v. Carson*, Civil Action No. 3:07-CV-1761-G, August 28, 2008 Memorandum Opinion and Order, 2008 U.S. Dist. LEXIS 68673 (N.D. Tex), at \*2 (TracFone’s assertion of “copyrighted and proprietary software computer code installed in the Phones”). The Court there described the importance of TracFone’s software:

Customers prepay for wireless service from Tracfone by purchasing "airtime cards." *Id.* PIN numbers located on the cards are entered into the specially manufactured phones to load airtime minutes. *Id.* The airtime cards are carried by national retailers such as Wal-Mart, Target, and Sam's Club. *Id.* Software installed onto the phones prevents their use without the loading of airtime minutes from a TracFone or NET10 airtime card. *Id.* P 25. TracFone's business model turns on its phones being used solely on the TracFone prepaid wireless network. *Id.* P 24. TracFone sells its phones for less than cost and "recoups this subsidy through profits earned on the sale of the Tracfone prepaid airtime cards that are required [\*3] to make and receive calls on the TracFone/NET10 Prepaid Phones."

*Id.* at 2-3 (emphasis added).

<sup>4</sup> [Verizon’s] Agreement for TracFone Wireless Inc., at 5. ¶ 2.3(ii). TracFone submitted this and the AT&T Mobility and T-Mobile agreements cited below under P.U. Code section 583, but has waived the protections of 583 to the extent set forth here.

<sup>5</sup> TracFone’s Reseller Agreement with AT&T Mobility, at 10.

software, technology, handsets, accessories or other materials or equipment used by [TracFone] in its business operation or by [TracFone's] End Users.”<sup>6</sup>

On August 20, 2008, TracFone filed an Advice Letter with this Commission, to which it attached a petition asking the Commission designate it as eligible for Federal universal service support (“Lifeline and Link Up Services to Qualified Households”) (Petition). Several parties filed comments or protests related to the Petition. In the course of investigating the issues raised by the comments and protests, staff of the Commission’s Communications Division (CD) discovered that TracFone had apparently never collected or remitted State universal service surcharges,<sup>7</sup> and had not paid required user fees since at least 2004.<sup>8</sup> On May 1, 2009, Staff requested that TracFone pay the amounts due;<sup>9</sup> TracFone refused,<sup>10</sup> and for that reason and others the Commission has denied TracFone’s Petition through Resolution (Res.) T-17235. Resolution T-17235, and a Staff Report published concurrently with this OII/OSC, set out further facts relating to TracFone’s failure to collect and remit the required surcharges and fees.

In response to a Communications Division data request, TracFone reported that it had California intrastate revenues in the following amounts for the following years:

2006 - \$ 57,176,752.00  
 2007 - \$ 63,503,404.00  
 2008 - \$ 62,022,339.00<sup>11</sup>

<sup>6</sup> [T-Mobile] Wireless Service Purchase Agreement, at Section 1.14 (emphasis added).

<sup>7</sup> P.U. Code §§ 270 *et seq.*, 701, and 739.3, *inter alia*, require the collection and remittance of such surcharges, as shown in the chart below.

<sup>8</sup> P.U. Code §§ 401-410 and 431-35 require the collection and remittance of such fees, as shown further in the chart below.

<sup>9</sup> May 1, 2009 email from CD staff to TracFone counsel, Attachment F to Staff Report; *see also* discussion in Staff Report at 6-8.

<sup>10</sup> May 15, 2009 letter from TracFone counsel to staff, Attachment H to Staff Report; *see also* discussion in Staff Report at 6-8.

<sup>11</sup> Staff Report, Attachment J.

Based on this reporting, and imputed numbers for 2004 and 2005, Staff reports that TracFone owes the State an aggregate total of over \$13,170,727 in surcharges, fees, interest and penalties (see Appendix A, attached hereto).<sup>12</sup>

### III. DISCUSSION

#### A. TracFone's Refusal to Collect and Remit Public Purpose Program Surcharges and User Fees Violates State and Federal Law.

California statute authorizes the Commission to set up various universal service programs to help extend telecommunications service to low-income, deaf and disabled, and rural (or other high-cost) customers,<sup>13</sup> and gives the Commission discretion as to the manner in which it collects and disburses funds to support these programs.<sup>14</sup> The Commission has established rules providing that State universal service contributions are to be collected from "all end users" of telephone services, including wireless services. In D.96-10-066, we

... reaffirmed the position which we took in D.94-09-065 at page 292. In that decision, we held that **all end users** of **every** LEC, IEC, **cellular**, and paging company in the state, receive value from the interconnection to the switched network, and that all users should be included in the billing base for the ULTS program and the Deaf and Disabled Telecommunications program.<sup>15</sup>

<sup>12</sup> *Id.* at Appendix A. A portion of Appendix A, addressed to the surcharge issue (which alone accounts for \$12.5 million of the monies owed), is attached hereto, likewise as Appendix A.

<sup>13</sup> *See, e.g.*, P.U. Code §§ 401 *et seq.*

<sup>14</sup> *See, e.g.*, P.U. Code § 739.3(c).

<sup>15</sup> Slip Op. at 287-88, 68 CPUC 2d at 622 (emphasis added). Ordering paragraphs 8(g) and 10(d) clarified the scope of this obligation (with reference to CHCF-B and Teleconnect programs):

All telecommunications carriers are required to charge **all end users** the ... surcharge as set by the Commission, except for ULTS billings, coin-sent paid calling, debit card messages, one-way radio paging, usage charges to COPTs, customers receiving services under existing contracts ... and directory advertising.

(Emphasis added.) Ordering paragraph 10(d) enunciated the same ruling for the California

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Separate and apart from “all end user” surcharges for universal service programs, statute authorizes the commission to collect from public utilities (and, more recently) cable companies a user fee “to fund Commission with (1) its authorized expenditures for each fiscal year ...; [and] (2) an appropriate reserve.”<sup>16</sup> For telephone corporations, that fee is calculated (like the public purpose surcharges) as a small percentage of intrastate revenue.<sup>17</sup>

In failing to collect and remit public purpose surcharges and user fees since at least 2004, TracFone appears to have violated California statutes that require all telecommunications carriers to collect and remit the following fees:

Public Purpose Surcharge or Fee	Statute
Universal Lifeline Telephone Service	§§ 270 <i>et seq.</i> , and 879
California Relay Service & Communications Device Fund	§§ 270 <i>et seq.</i> , and 2881
California High Cost Fund A (CHCF-A)	§§ 270 <i>et seq.</i> , and 739.3
California High Cost Fund B (CHCF-B)	§§ 270 <i>et seq.</i> , and 739.3
California Teleconnect Fund	§§ 270 <i>et seq.</i>
California Advanced Services Fund (CASF)	§ 701 <sup>18</sup>
Calif. Public Utilities Commission User Fees	§§ 401-410, 431 – 435

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Teleconnect Fund. As noted, these determinations were a continuation of the Commission’s rulings in the Implementation Rate Design (IRD) proceeding, which adopted proposals to include the customers of wireless service providers in the “billing base” against which universal service surcharges are assessed. *See* D.94-09-065, 56 CPUC 2d 117, 266, 285, and Conclusions of Law 230-32 (“Application of a surcharge to the widest possible customer base is fairer to all competitors ...”); *see also id.* at 290 (Ordering Paragraphs 71 & 72).

<sup>16</sup> P.U. Code § 401; *see also* D.07-03-014 (user fees for DIVCA franchisees).

<sup>17</sup> P.U. Code § 432(c)(3).

<sup>18</sup> This fee was instituted by SB 1193 (Chapter 393, Statutes of 2008), and only applies to revenue collected on or after January 1, 2008.

Federal statute also requires all providers of telecommunications service contribute to universal service programs:

*All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.*<sup>19</sup>

Federal statute specifically requires telecommunications carriers to contribute to State universal service programs in addition to the Federal programs:

Every telecommunications carrier that provides intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, in a manner determined by the State to the preservation and advancement of universal service in that State.<sup>20</sup>

As set forth in Resolution T-17235, we do not find TracFone's claim that it is a 100% reseller, with no facilities of its own, and therefore exempt from the surcharge and fee obligations to which all other telephone corporations are subject, to be either credible or tenable. The Commission regularly imposes utility regulation on "pure" resellers of landline service,<sup>21</sup> and requires both competitive local exchange carriers (CLECs) and inter-exchange carriers (IXCs), even if resellers, to pay user fees and public purpose surcharges.<sup>22</sup> The letter granting TracFone's predecessor a wireless registration number specifically conditioned that grant on the carrier's compliance with all Public Utilities Code sections applicable to telecommunications carriers, including the payment of such fees and surcharges.<sup>23</sup>

<sup>19</sup> 47 USC § 254(b)(4) (emphasis added).

<sup>20</sup> 47 USC § 254(f); *see also WWC Holding Co. v. Sopkin*, 488 F3d 1262, 1277 (10<sup>th</sup> Cir., 2007) ("The structure of Section 254 of the Telecommunications Act delineates a federal universal service program . . . and a state's authority to create its own such program") (citations omitted).

<sup>21</sup> *See, e.g., Investigation of Clear World*, D. 05-06-033, Slip Op. at 2, O.P. 1 (\$100,000 fine for unauthorized re-sale of long distance service); *see also* discussion in Resolution T-17235.

<sup>22</sup> *See, e.g., D.05-06-033*, at O.P. 2(f) (investigation into reseller's failure to pay required fees and surcharges).

<sup>23</sup> July 18, 1997 Commission letter to Topp Telecom, Inc., *supra*, at 1 ("In all respects except for

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To date, TracFone has provided no credible rationale why it should not now be ordered to pay all delinquent user fees and public purpose surcharges, and fined for its violation of California law requiring timely remittance of such fees and surcharges.<sup>24</sup>

**B. Categorization**

This proceeding is categorized as adjudicatory. *Ex parte* communications are prohibited. The determination as to category is appealable under Rule 7.6 of the Commission's Rules of Practice and Procedure

Good cause appearing,

Therefore, **IT IS ORDERED** that:

1. An investigation is instituted on the Commission's own motion to determine whether Respondents violated any provision of the Public Utilities Code, or our general orders, other rules, or requirements by failing and refusing to pay public purpose surcharges and user fees;

2. Respondent TracFone shall appear and show cause why the Commission should not find that:

- a. it is in violation of the statutes and other authority cited herein requiring all California telecommunications utilities to collect from all end users, and remit to the Commission, public purpose surcharges and user fees;

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market entry and rates, the authority of the Commission to regulate terms and conditions of newly registered cellular carriers shall apply to the same extent as those holding certificates of CPCN prior to August 10, 1994”).

<sup>24</sup> TracFone's arguments against application to it of a surcharge and user fee obligation have been contained in TracFone correspondence, and in its Comments on Draft Resolution T-17235, which are summarized and addressed in the final form of that Resolution.

- b. it owes monies to the various public program funds described in this Order for unpaid surcharges, and to the Commission for unpaid user fees, in amounts as shown in the accompanying Staff Report; and
- c. it should be fined pursuant to P.U. Code §§ 2107 and 2108 for the above-described violations of the Public Utility Code and related Orders, Decisions, and Rules.

3. Respondents are put on notice that the Commission may order the implementation of reporting and collection measures designed to prevent future violation of the statutes cited herein.

4. Pursuant to Rule 7.1(c) of the Commission's Rules of Practice and Procedure, this proceeding is categorized as adjudicatory, and this Order constitutes a preliminary scoping memo. The categorization of this Order is appealable under Rule 7.6.

5. A prehearing conference shall be convened before an Administrative Law Judge (ALJ) for the purpose of establishing a schedule in this matter including (if necessary) dates for the exchange of additional written testimony, and (to the extent necessary) dates for evidentiary hearings and briefing in this matter.

6. The attached Staff Report prepared by the Commission's Communications Division is hereby entered into the record for this proceeding.

7. To facilitate the completion of this investigation, and consistent with the provisions of P.U. Code § 314, respondents are ordered to preserve until further notice all documents, regardless of age, which might relate to this action, including but not limited to all internal accounting, inter-company transfers and the like.

8. Other utilities, from which TracFone obtains the network facilities necessary to its telephony business in California and/or with which TracFone transacts business, are ordered to cooperate with Staff in its investigation, and provide documents and witnesses as requested, during the pendency of this action.

9. The Staff shall continue to investigate the operations of Respondents. The cutoff date for advancing evidence of additional violations, and for the exchange of



testimony, shall be determined by the Assigned Commissioner or Assigned Administrative Law Judge.

10. Staff shall be subject only to discovery relating to the specific violations alleged in this order, or those added by subsequent motion.

11. Any person filing a response to this OII/OSC shall state in the response any objections to the order regarding the need for hearings, issues to be considered, or proposed schedule. Such objections should be confined to jurisdictional issues that could nullify any Commission decision on the issues set out herein, and not consist of factual assertions more properly the subject of evidentiary hearings.

12. The Executive Director shall cause a copy of this Order to be served by certified mail on Respondent TracFone at:

Corporate Creations Network Inc.  
131-A Stoney Circle, Suite 500  
Santa Rosa, CA 95401

In addition, Staff shall serve by electronic service copies of this OII and the attached Staff Report on TracFone's counsel of record in this and the related ETC matter.

This order is effective today.

Dated: December 17, 2009, in San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH  
JOHN A. BOHN  
TIMOTHY ALAN SIMON  
Commissioners

Commissioner Rachelle B. Chong, being necessarily absent, did not participate.