

Before the  
United States Senate  
Committee on Commerce, Science, and Transportation

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**Statement of Mr. Arturo “Archie” Macias,  
General Manager, Wheat State Telephone Company,**

**on behalf of the**

**Organization for the Promotion and Advancement of  
Small Telecommunications Companies**



**O P A S T C O**

**In the Matter of  
*S. 2281, “The VOIP Regulatory Freedom Act of 2004”*  
June 16, 2004**

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## **Introduction**

Chairman McCain, Ranking Member Hollings, members of the committee, my name is Archie Macias, and I am the General Manager of Wheat State Telephone Company, an independently-owned telecommunications provider based in Udall, Kansas. My company provides telecommunications and Internet services to the Kansas communities of Udall, Rock, Olpe, Matfield Green, Cassoday, and Potwin. Wheat State also offers “High-Speed Xcelerator,” a high-quality broadband service utilizing Digital Subscriber Line (DSL) technology. At present, we have been able to deploy this service to 90 percent of our customers with a “take rate” of about 11 percent. Wheat State is truly a small, rural carrier. We serve approximately 2,300 customers over 750 miles of territory, with a population density of three per square mile. Two of my exchanges are located in the Flint Hills, where there are more cattle than customers.

I am very proud of Wheat State’s commitment to providing exceptional quality basic and advanced communications services at affordable rates. By doing so, we contribute to economic development and improve the quality of life for the communities and citizens of rural Kansas. However, Wheat State's commitment to providing service to a very rural part of the country is not unique. There are hundreds of rural telephone companies nationwide that are just as committed to providing superior service to rural consumers.

This morning, I am particularly pleased to appear before you on behalf of more than 560 rural carriers across 46 states that are represented by the trade association that I presently chair, the Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO). OPASTCO members are among the industry leaders in bringing new, innovative services to consumers in high-cost rural areas. For instance, a recent OPASTCO member survey found that respondents, on average, have been able to make broadband available to 88 percent of their customers and more than half of the respondents have made broadband available to at least 95 percent of their customers.

Mr. Chairman, I am pleased to participate in this hearing regarding Senate Bill 2281, “*The VOIP Regulatory Freedom Act of 2004.*” If committee members take just one point from my remarks, let it be this: Rural consumers will not be able to enjoy the benefits of Voice over Internet Protocol (VoIP), if the underlying networks operated by rural telephone companies are compromised due to a lack of adequate cost recovery.

### **Legislation Restricting Rural Carriers’ Ability To Recover The Costs Of Providing Access To Their Networks Would Impede The Deployment Of Broadband And VoIP In Rural Areas**

Mr. Chairman, the most troubling aspect of S. 2281 is that it places an explicit ban on the application of access charges to VoIP services. Instead, the legislation allows for cost recovery through reciprocal compensation, which only covers a fraction of rural telephone companies’ costs of providing access; or through bill-and-keep, which is another way of saying “free.” While reciprocal compensation or bill-and-keep might be

acceptable for large carriers serving tens of millions of customers across many states, neither is suitable for small carriers with only several thousand or fewer customers. Legislation that takes a “one-size-fits-all” approach and treats urban and rural areas the same clearly will not work.

Rural telephone companies rely heavily on interstate and intrastate access charges to recover the costs of supplying other service providers with access to their facilities. In fact, rural telephone companies, on average, recover 26 percent of their total costs from carrier access charges. It is important to note that the use of IP technology for a voice call does not in any way reduce the costs of providing access to a rural telephone company’s local network. If rural telephone companies are prohibited from recovering their full costs of providing access services to others, either through below-cost reciprocal compensation or the free bill-and-keep method, the remaining costs could be borne solely by the telephone company’s limited customer base, many of whom may not even choose to use VoIP services. These costs will be reflected through reduced service quality, higher rates, or both.

Small rural carriers already face operational challenges such as sparsely populated service areas and a lack of economies of scale, both of which result in higher per-customer costs. Yet rural telephone companies are making great strides deploying broadband technology, such as DSL, wherever possible, even as they maintain and enhance the highly reliable Public Switched Telephone Network (PSTN) that so many people depend upon. Rural carriers are committed to continue providing high quality services on both the public switched and broadband networks they deploy, but they need full cost recovery to accomplish this goal.

Until the transition to a new IP network is complete in ten to fifteen years, both networks need to be maintained and paid for. If the PSTN is neglected and VoIP providers become unable access customers through the PSTN, then the value and efficiency of VoIP as a new technology would be significantly lower. Thus, **all** customers would suffer. Without the cost recovery made possible through access charges, the ability of rural telephone companies to continue investing in the network upgrades necessary to provide broadband to greater numbers of customers would be seriously compromised. Since broadband is generally necessary to carry VoIP services, a prohibition on access charges would have the ironic effect of preventing VoIP service providers from making their services available to some consumers in rural areas. Obviously, this is the exact opposite of the legislation’s intent.

OPASTCO wholeheartedly agrees with the Federal Communication Commission’s (FCC) recent statement that:

... any service provider that sends traffic to the PSTN should be subject to similar compensation obligations, irrespective of whether the traffic originates on the PSTN, on an IP network, or on a cable network. We

maintain that the cost of the PSTN should be borne equitably among those that use it in similar ways.<sup>1</sup>

Moreover, if all service providers that utilize rural telephone companies' networks do not pay for access in a similar manner, regulatory arbitrage will occur. In a recent Order, the FCC correctly stated that "IP technology should be deployed based on its potential to create new services and network efficiencies, not solely as a means to avoid paying access charges."<sup>2</sup> Further, as FCC Chairman Michael Powell observed in the same Order:

To allow a carrier to avoid regulatory obligations simply by dropping a little IP in the network would merely sanction regulatory arbitrage and would collapse the universal service system virtually overnight.<sup>3</sup>

Rural consumers should have access to IP-enabled services, including VoIP services, that are comparable in quality and price to those provided in urban areas, as called for by the Telecommunications Act of 1996 (1996 Act). If rural telephone companies are to maintain a modern infrastructure capable of delivering VoIP and other services at affordable rates, they cannot be expected to supply access to their local networks to other service providers for free or for less than their own costs.

### **The Appropriate Regulation Of VoIP Should Be Determined In The Context Of Several Comprehensive Proceedings Currently Being Conducted By The FCC, Not In Stand Alone Legislation On VoIP**

Mr. Chairman, OPASTCO greatly appreciates the keen interest that Congress has taken in the deployment of broadband and VoIP in recent years. However, at this time we believe that S. 2281 is premature. Important as VoIP services are, they are but one component of several interrelated and comprehensive proceedings already underway at the FCC. One of these proceedings is examining the appropriate regulatory environment for IP-enabled services, including VoIP (WC Docket No. 04-36). Another is considering wholesale reform of the current intercarrier compensation regime (CC Docket No. 01-92), which many parties agree is outdated, in part because of new services such as VoIP. And yet another proceeding is considering both the legal classification of wireline broadband Internet access as well as whether to require all broadband Internet access providers to contribute to universal service (CC Docket No. 02-33). Congress should not short-circuit this comprehensive approach.

Through these proceedings, the FCC will be able to benefit from the input of the industry, consumer interests, state regulators, and other parties before rendering judgement on these interrelated and highly complex areas of communications policy. Certainly,

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<sup>1</sup> *IP-Enabled Services*, WC Docket No. 04-36, Notice of Proposed Rulemaking, FCC 04-28 (rel. Mar. 10, 2004), paras. 33, 61.

<sup>2</sup> *Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony Services are Exempt from Access Charges*, WC Docket No. 02-361, Order, FCC 04-97 (rel. Apr. 21, 2004), para. 18 (AT&T Order).

<sup>3</sup> *Ibid.*, Statement of Chairman Michael K. Powell.

Congress should continue to fulfill its critical oversight role, and ensure that the FCC adopts policies that serve the interests of all Americans, especially those living in rural areas which face the greatest impediments to the deployment of advanced services.

OPASTCO fully recognizes that the FCC's open proceedings may change the manner in which rural telephone companies recover the costs of other providers' use of their networks. However, before changes to the existing mix of intercarrier charges, end-user charges, and universal service can be adopted, there needs to be a thorough examination of the impacts on high-cost rural telephone companies and their customers. Until this process is complete, VoIP service providers that interconnect with the PSTN should provide equitable compensation for their use of rural telephone companies' networks through duly approved access charges.

### **The Base Of Universal Service Fund Contributors Should Be Expanded To Include All Facilities-Based Broadband Internet Access Providers**

Mr. Chairman, OPASTCO is pleased to see that S. 2281 includes a provision that grants the FCC the necessary authority to ensure the preservation and advancement of federal universal service programs, in light of the growth of services such as VoIP. As OPASTCO has stated on numerous occasions, both before this Committee and directly to the Commission, the best way to accomplish this important goal would be to require all facilities-based broadband Internet access providers to contribute to the Universal Service Fund (USF).

In Section 254 of the 1996 Act, Congress called for specific, predictable, and *sufficient* mechanisms to preserve and advance universal service. As the marketplace evolves toward broadband platforms and IP networks, the shift away from more traditional telecommunications services will continue to "drain" the support base for universal service, threatening its sufficiency. This impact is even more pronounced when providers offer voice services over broadband platforms that are the functional equivalent of traditional telephony, but the underlying broadband access provider is not required to contribute to universal service.<sup>4</sup> Thus, as FCC Commissioner Jonathan Adelstein recently noted, the rapid evolution of IP-enabled services might drain substantial amounts of support for the local network providers in high-cost areas that enable rural consumers to enjoy these types of services.<sup>5</sup> While the accelerating use of broadband platforms and IP networks may offer certain benefits, it also plays a significant role in the present instability of the USF contribution base.

Mr. Chairman, extending universal service assessments to all facilities-based broadband Internet access providers would greatly alleviate this danger. Doing so would help keep

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<sup>4</sup> See, *Federal and State Universal Service Programs and Challenges to Funding*, Report to the Ranking Minority Member, Subcommittee on Telecommunications and the Internet, Committee on Energy and Commerce, House of Representatives, General Accounting Office (rel. February 2002), p. 21-22 (GAO Report): "As the deployment of IP telephony technologies move forward, and more businesses and consumers begin to substitute IP telephony for traditional telephone service, the question arises as to whether a decline in the funding for universal service could result."

<sup>5</sup> See, AT&T Order, Statement of Commissioner Jonathan S. Adelstein.

the USF sustainable for the long term, even as increasing amounts of voice traffic migrate away from traditional telecommunications carriers. This, in turn, would help to ensure that consumers in rural and high-cost areas continue to have affordable access to telecommunications and information services, including advanced services, that are comparable to those offered in urban areas, as the 1996 Act demands. Furthermore, when some service providers are not required to contribute to universal service, the obligation upon those who are required to contribute is obviously greater. Spreading support obligations as widely as possible reduces each company's contribution, which, in turn, reduces the level of universal service assessments that each carrier must ultimately pass on to their customers.

Moreover, the FCC's own universal service principle of competitive neutrality requires that facilities-based broadband Internet access providers over all platforms contribute to universal service. Currently, only wireline telecommunications carriers are required to contribute on revenues earned from their DSL-based broadband transmission service. Cable modem, satellite, and other broadband platforms are not presently required to contribute. Broadband Internet access providers that are exempt from contributing to universal service have a competitive advantage over those who are required to contribute, as they do not need to recover any support payments from their end users.<sup>6</sup> By expeditiously requiring facilities-based broadband Internet access providers over all platforms to contribute, it would also eliminate the growing inequity and potential for marketplace distortions that arise under the current rules.

### **IP-Enabled Services That Are Functionally Equivalent To Traditional Telephony Should Be Subject To Similar Service Obligations**

Mr. Chairman, OPASTCO is pleased to see that S. 2281 acknowledges the need for VoIP providers to be subject to certain social obligations such as enhanced 911 functionality and compatibility for the disabled community. However, for those VoIP providers that are offering service that is functionally equivalent to traditional telephony, we believe that these types of obligations should be mandatory, not voluntary as the bill suggests. In its 1998 Report to Congress on Universal Service, the FCC correctly stated that "the classification of a service under the 1996 Act depends on the functional nature of the end-user offering."<sup>7</sup> Similarly, FCC Chairman Michael Powell has declared that:

[S]ound regulatory policy should, where appropriate, harmonize regulatory rights and obligations that are attached to the provision of similarly situated services across different technological platform[s].<sup>8</sup>

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<sup>6</sup> See, GAO Report, p. 22, fn. 31: "IP telephony calls, which do not include universal service charges [which, for large companies average between 8 to 12 percent of the total telephone bill] can mean a savings of around 10 percent on corporate telephone bills. This savings ... may make IP networks attractive to large business end users."

<sup>7</sup> *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report to Congress, 13 FCC Rcd, 11501, 11543, para. 86 (1998).

<sup>8</sup> Remarks of Michael K. Powell, Chairman, Federal Communications Commission, at the Broadband Technology Summit, US Chamber of Commerce, Washington, D.C. (April 30, 2002).

While IP-enabled services should not be subject to disproportionate or unnecessary burdens, neither should end-users find themselves lacking access to important features that they have come to expect from all providers of telephone service. For instance, consumers have a right to expect E911 functionality from all service providers that offer functional equivalence to traditional telephony, regardless of whether or not the service is IP-enabled, and regardless of whether the service may offer other types of enhanced features. Similarly, the use of different technological platforms should not deny consumers with disabilities the same choices among service providers as others.

Moreover, a competitive disparity will result if one set of carriers are held to public safety and disability access standards, but other service providers offering functionally equivalent services over different technological platforms are not. Not only would this present another arbitrage opportunity, it would also make it more difficult for service providers with these obligations to fulfill their responsibilities as they lose customers to competitors that do not have the same public service requirements. It is not justifiable to risk public safety and limit choice for the disabled in order to provide a competitive advantage to a subset of providers that offer service that is functionally equivalent to traditional telephony, based on their use of a particular technology.

### **Rural Telephone Companies Must Retain The Option To Include DSL In Revenue Pools, Regardless Of How It Is Statutorily Classified**

Mr. Chairman, currently, the FCC classifies services delivered via DSL technology as “telecommunications services.” However, in February 2002, the FCC initiated a proceeding in which it tentatively concluded that the legal classification of DSL-based services should change to “information services.” In the event that changes in the legal classification of wireline broadband Internet access lead to the phase-out or elimination of tariffing for DSL-based services, some type of effective pooling mechanism must remain available. For many rural telephone companies, the provision of advanced services at affordable rates would not be viable without participation in the revenue pools administered by the National Exchange Carrier Association (NECA). In fact, in a recent OPASTCO survey of its members, more than 60 percent of the respondents indicated that they utilize the DSL tariffs available in the NECA pools.

Pooling enables these carriers to offer DSL-based services to consumers under tariffed rates that are based upon pool-wide averaged costs. Pool participants remit the revenues generated from their DSL-based services to the pool, and are able to recover their actual costs through the NECA pools. Thus, the provision of advanced services at affordable rates in many high-cost rural areas would simply not be possible without pooling. However, if a change in the legal classification of DSL led to a prohibition on tariffing, without careful planning and foresight by the FCC, many rural telephone companies could find themselves without any pooling mechanism for their broadband Internet access service.

Investment in DSL-capable infrastructure is risky for rural carriers because of low population density and other factors that make service more costly to provision in these

markets. Many rural telephone companies deployed DSL technology with no reason to believe that pooling might be discontinued in the foreseeable future. Pooling remains necessary in order for them to recover the considerable costs of deployment and continue providing the service.

An elimination of DSL from the NECA pools could require significant rate increases, which might force some customers of rural carriers to stop subscribing to DSL-based services that they currently enjoy. It could also leave these carriers with significant stranded investment and financial losses. Further, pooling carriers would find it far more difficult, and in many cases impossible, to expand DSL-based services to consumers who are located further from the rural telephone company's central office. Obviously, these outcomes would be antithetical to the goal of Congress and the FCC to encourage the ubiquitous availability of advanced services to all Americans. Therefore, no matter how the FCC ultimately decides to statutorily classify wireline broadband Internet access, it is imperative that rural telephone companies retain a pooling option for their DSL-based services.

**If Federal Jurisdiction Is Asserted Over VoIP, It Is Essential That The Process Is Revenue-Neutral For All Rural Telephone Companies In All States, Without Prejudice To a State's Rate Rebalancing Efforts**

Mr. Chairman, as you know, S. 2281 reserves to the federal government the sole responsibility and authority to regulate the offering or provision of VoIP applications. While OPASTCO does not oppose the assertion of federal jurisdiction over VoIP, were this to occur, it is critical that Congress ensure that the process is revenue neutral for all rural telephone companies in all states.

As I discussed earlier, rural telephone companies derive a significant portion of their revenues from access charges, both interstate and intrastate. States are far from uniform in how they allow rural telephone companies to recover their intrastate access costs. Many have engaged in rate rebalancing to various degrees, while other states have not rebalanced at all. This results in a wide range of local end-user rates and intrastate access rates among rural telephone companies in different states. Some states have relatively low local end-user rates, but with intrastate access rates that make up the difference in the rural phone companies' intrastate costs. Other states have significantly lowered intrastate access rates, but have offset these reductions through much higher local end-user rates.

Therefore, in the event that federal jurisdiction is asserted over IP-enabled services, Congress and the FCC must ensure that the process is revenue-neutral for all rural telephone companies in all states, without prejudice to a state's rate rebalancing efforts. Before rural carriers can make investments in their network, they need reasonable assurances that they will be permitted to recover the costs of those investments. No rural telephone company should be denied full recovery of its costs on account of a state commission's end-user and intrastate access rate policies – decisions over which rural carriers have little, if any, control.

Moreover, full cost recovery must be permitted in a manner that does not threaten the stability and sustainability of existing high-cost support mechanisms. In the 1996 Act, Congress directed that end-user rates remain affordable and that there is reasonable comparability between rural and urban rates and services. However, both policymakers and service providers share concerns regarding the impact that substantial growth of the existing high-cost component of the USF would have on its sustainability. Therefore, should federal jurisdiction be asserted over VoIP, there must be a thorough analysis of the potential ramifications such an action might have for end-user rates, and a sufficient support mechanism must be put in place that would fulfill Congress' universal service objectives. As I discussed previously, one step that can be taken to that end is to expand the base of USF contributors to include all facilities-based broadband Internet access providers.

## **Conclusion**

Mr. Chairman, OPASTCO appreciates the interest and efforts that Congress has taken over the past several years in encouraging the deployment of advanced services throughout the nation, and to rural areas in particular. Without a doubt, VoIP and other advanced services have the potential to deliver innovative features to rural consumers. However, we believe that legislation regarding VoIP is premature at this time. The FCC currently has open proceedings on IP-enabled services, intercarrier compensation and universal service, among others. Through these proceedings, the FCC will be able to benefit from the comments of the industry, consumer interests, and other parties before rendering judgement on these interrelated and highly complex areas of communications policy.

OPASTCO members are among the industry leaders in bringing new, innovative services to consumers in rural areas. If Congress seeks to continue encouraging infrastructure and service deployment in rural areas, it must ensure that the underlying networks that deliver voice, data and video to consumers remain reliable. Thus, it is essential that the regulatory treatment of VoIP applications not inadvertently compromise the existing PSTN or the build-out of broadband platforms in rural areas, which are necessary for the delivery of these services. Mr. Chairman, thank you for giving me the opportunity to testify on this issue which greatly impacts rural telephone companies and our ability to continue providing high-quality, modern service to our customers.