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April 3, 1998

VIA HAND DELIVERY

Magalie Roman Salas
Secretary
Federal Communications Commission
Room 222
1919 M Street, NW.
Washington, DC 20554

Re: *Ex Parte* Submission in CC Docket 96-45, Report to Congress on Universal Service under the Telecommunications Act of 1996.

Dear Secretary Salas:

On Thursday, April 2, 1998 Steve Stewart of IBM Corp. and myself, on behalf of the Internet Access Coalition, met with James Casserly, Senior Legal Advisor to Commissioner Ness, to discuss the proposal regarding Universal Service contributions made by the Commissioner during her March 30th speech before the Information Technology Association of America regarding Universal Service contributions. A copy of the Commissioner's speech is enclosed.

Pursuant to 47 C.F.R. Section 1.1206(a)(1) two copies of this letter are being filed with the Secretary of the Commission today.

Respectfully submitted,

Colleen Boothby

Counsel for
The Internet Access Coalition

Enclosure

290.01/Stevens Report/LTR Ex Parte re RPT to Congr.doc

Remarks of
Commissioner Susan Ness
Before the Policy Summit of The
Information Technology Association of America
Washington, D.C.
March 30, 1998

"Making Sense"

(as prepared for delivery)

Good morning.

There is nothing more magnificent than spring in Washington. I hope that you have had a chance to enjoy the cherry blossoms. Energy and optimism are in the air.

Energy and optimism are the hallmark of your industry. So I am especially pleased to talk with you this morning.

This is a pivotal time. Right now, we at the Federal Communications Commission are thinking a lot about information technology and information services.

At the specific directive of Congress, we are reassessing the Commission's past decisions regarding the definitions of "information services," "telecommunications," and related terms. We are evaluating whether these decisions are consistent with the Telecommunications Act of 1996.

In this context, we are seeking to better understand the evolution of computer and information technologies, and the services offered by carriers and by information service providers. Computer ownership is growing, and demand for bandwidth is growing faster still. Digital technologies continue to supplant analog. Packet switching is rapidly gaining on circuit switching. Billions of dollars are being invested in new facilities and services.

In light of all that has happened, is happening, and is likely to happen in the laboratory and in the marketplace, we need to ensure that the Commission's policies and rules are ones that make sense.

Do they promote competition? Do they stimulate innovation? Do they promote the deployment of desirable technologies? Are they internally consistent? Are they sustainable? Are they as minimally regulatory as possible? And, of course, do they comport with the law as Congress wrote it?

I want to address these questions in greater detail, but first I want to set the stage.

The Computer-Friendly FCC

I want to begin by saluting my predecessors at the Commission, whose policies have contributed greatly to the growth and health of the information services industry.

It is hard to believe that there could be three decades of debate on a single topic. But so there has. The issue is the appropriate regulatory treatment of services that employ computer processing capabilities to "enhance," or add value to, the basic communications network.

In the Computer Inquiry, the Second Computer Inquiry, and the Third Computer Inquiry, we repeatedly confronted the same fundamental issue: which Title II regulations, if any, should apply to services that combine computer processing with pure transmission to provide "value-added" applications? That same question is with us today.

In the past inquiries, the central question was always the same, but the context was different. Thanks to Moore's Law, the price-performance ratio of computer processing has been changing geometrically, year after year. The use of computers *in* the telephone network (as switching devices) has grown by leaps and bounds, and the connection of computers *to* the telephone network has soared from hundreds to thousands to millions to tens of millions.

Throughout this evolution, the Commission has recognized the value of enhanced services and has been careful to act in ways that facilitate innovation and growth.

Long before the Telecommunications Act of 1996 expressed Congress's desire to pursue "pro-competitive, de-regulatory" policies for telecommunications, the Commission applied precisely this approach to enhanced services.

And so, in Computer II, almost 20 years ago, the Commission decided that enhanced services should be outside the scope of Title II regulation. In subsequent years, we reaffirmed this determination. We treated providers of enhanced services, not as carriers, but as users of communications services.

This meant no tariff requirements. No entry and exit regulation. We resisted entreaties that ESPs should pay the carrier's carrier charges that interexchange carriers pay when they originate or terminate traffic over local telephone companies' facilities. And we resisted proposals that could have limited user choice in the equipment they connect to the telephone network.

These decisions have been revisited on a variety of occasions, and in a variety of settings, but the bottom line has remained the same: promote competition, and avoid regulation.

Thus, I think it's beyond dispute that the Commission has been computer-friendly for a long period of time. And it's equally clear that the businesses and consumers of America have reaped the rewards.

Think a minute: Voice mail. E-mail. Alarm monitoring. Database services. Credit card processing. Automatic teller networks. On-line services.

And the list goes on.

So, the record is pretty clear that the Commission's past decisions have worked pretty well. But just the same, it's entirely appropriate to take a fresh look.

Why? Well for one thing, Congress told us to. That, in and of itself, is an entirely sufficient answer.

But it's not the only reason. Two others are the fundamental changes that are happening in telecommunications regulation and the explosion of new IP-based services.

The Competition Trilogy

First, as to changes in telecommunications regulation: As you know, Congress passed a new law two years ago that caused the most sweeping changes in the Communications Act since 1934.

This statute had many facets, but the single biggest change intended by the new law was to replace

monopoly with competition in the local telephone market. To this end, Congress enacted specific "interconnection" requirements, regarding the ways in which new entrants could use, or connect with, the services and facilities of the incumbent carrier's network.

Even as Congress sought to introduce local competition, it also intended to preserve universal service.

It has long been a goal of telecommunications policy that quality services be available at affordable prices throughout the nation. We have long had programs to assist low-income consumers and consumers in high-cost areas to acquire telephone service.

But these programs are not competitively neutral in how the support is collected or distributed. They rely on a web of implicit subsidies that is not sustainable in a competitive market.

And so, the Commission sought to establish -- as Congress required -- new support mechanisms that are explicit, sufficient, predictable, and competitively neutral. At the same time, the Commission implemented Congress's decision to expand the notion of universal service. No longer is it focused solely on supporting low-income and high-cost consumers. Now, it also encompasses targeted support for schools, libraries, and rural health care providers.

Coincident with changes in competition and in universal service, the Commission has also sought to reform interstate access charges. The goal is to enable cost recovery in a more economically efficient manner and to harness market forces to drive prices closer to cost.

All of these changes are still in progress. But meanwhile, the markets are changing before our eyes.

The explosive growth of IP-based services is perhaps the most startling phenomenon. While voice traffic increases at a modest pace of 8 or 10 percent a year, data traffic is skyrocketing. This is cause for excitement in some quarters, cause for alarm in others.

Local telcos complain that data calls typically last much longer than voice calls, tying up switches and requiring the addition of more capacity in the loop and the central office. Long distance companies worry that new IP telephone services will undercut them in the market because they can avoid access charges and universal service support obligations. Legislators from high-cost regions express concerns that anomalies in the existing rules will cause a migration of traffic from services that bear a universal service support obligation to services that do not carry this burden.

The "Universal Service Report"

These are not frivolous concerns. We are obligated to revisit these issues and address the concerns raised. And that's just what we're doing in the context of our Universal Service Report.

An appropriations measure passed by Congress last fall, at the urging of Senator Stevens, requires the Commission to review the statutory definitions of "telecommunications," "information services," and related terms. It directs us to evaluate the impact of the Commission's interpretations of these terms on the provision of universal service.

This inquiry will be rooted, first and foremost, in the words of the statute and the legislative history. To the extent Congress has answered a question, our inquiry need proceed no further. But to the extent Congress has left us with discretion, we need to figure out what makes the most sense.

I hear two main lines of argument. One is that Congress radically changed the dichotomy that was established in Computer II and essentially replicated in the Modification of Final Judgment. Under this line of argument, information services are now a subset of telecommunications services and

subject to all of the provisions of Title II of the Communications Act.

A variation of this argument is that information services and telecommunications services no longer constitute a dichotomy but overlapping groups. As a result, some, but not all, information services are subject to Title II regulation.

The other main line of argument is that Congress enshrined the basic-enhanced dichotomy in law. Under this theory, enhanced services must remain unregulated, and ESPs should be able to avoid any of the obligations imposed on telecommunications carriers -- including universal service obligations and the requirement to pay access charges -- no matter how substitutable their services are for those offered by telecommunications carriers. And when communications and information processing are combined, the entire package is "contaminated" and beyond the reach of the communications law.

A variation of this argument holds that, perhaps some new services -- like Internet telephony

-- ought to be subject at some future date to certain Title II obligations, but it's really too soon to do anything about this. We should watch and wait and then, later, if the anomalies become too great, we should step in and impose universal service support obligations.

I doubt that your industry would be pleased if the first line of argument were to prevail. I doubt that legislators who are concerned about the future of support for high-cost areas would be too happy with the second.

For myself, I think there may be other alternatives. In particular, I am trying to understand better the ramifications of the "contamination doctrine" and to consider whether it is the source of market distortions.

Can a carrier escape its Title II responsibilities by adding a dollop of information services to what previously was a communications service? Clearly not. We've answered that question already. Less clear, however, is the treatment of the converse situation -- where an information service provider adds telecommunications services to the package it offers to consumers.

Now of course most information service providers procure their transmission services from carriers. America On-Line, I am told, has a billion-dollar phone bill, and those purchases help to support universal service. What if AOL substitutes self-supply for third-party supply for its transmission links? Are the links now "contaminated" and free of a universal service support obligation? If so, won't we create artificial incentives for vertical integration? Won't we distort the economics of the buy-versus-build decision?

I am tentatively thinking that no information service can move a bit from here to there without "riding on a rail" of telecommunications. That doesn't mean that a company supplying such capacity to itself necessarily needs to be classified as a "carrier," with all the attendant consequences. But it would mean that the universal service support obligation would be shared by all transmission lines.

I haven't thought this all the way through. You're getting a "real-time" update on my thinking. But I want you to understand that these are the kinds of questions we are intensely considering, and debating, now and until April 10, when we must file our report with Congress.

I encourage ITAA and its members to remain active in the debate, and in any rulemakings that follow. It is important that we make decisions that safeguard universal service, but avoid unnecessary regulation.

Section 706 Petitions

I also want to introduce another subject that I suspect will be of interest to you: bandwidth.

You've all heard the updated version of the old adage: "You can never be too rich or too thin, *or have too much bandwidth.*"

The issue of bandwidth in the local loop is becoming a major concern. As usage of the Internet soars, and Web pages are increasingly rich in graphical and even video rather than just textual data, users are increasingly frustrated by the performance of 28.8 or even 56 kbps modems. To support video, transmission speeds must be increased by a hundred-fold -- to the speeds made possible by technologies like cable modems and xDSL.

The good news is, these technologies already exist. The bad news? They aren't available to most consumers.

We need to figure out why.

As you may know, Congress directed the FCC to foster the deployment of "advanced telecommunications capability" throughout the nation. Advanced communications capability is defined in Section 706 of the statute as "high-speed, switched, broadband telecommunications capability that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology."

The statute directs the Commission to promote these capabilities by using forbearance, price cap regulation, competition, and other tools. It also directs the Commission to initiate an inquiry, no later than August 8, 1998, to evaluate whether the desired capabilities are being deployed.

Already, we have received petitions under Section 706 suggesting that FCC regulatory policies are standing in the way. We'll need to review those petitions carefully and the comments of interested parties and then figure out whether there is more the FCC can and should be doing to promote the deployment of bandwidth.

I encourage you to participate in this debate.

Conclusion

Universal service and bandwidth are but two of the major issues currently before the Commission. We're also increasing our focus on consumer protection issues: the scourge of slamming and cramming. We're pressing ahead to reform international accounting rates, and to ensure effective implementation of the historic WTO agreement. We're conducting a biennial review of numerous regulations that affect telecommunications providers. And we're spending a lot of time working with the Bell companies, and their would-be competitors, to fulfill market-opening responsibilities that are a precondition for Bell company offering of long distance services.

Many changes are underway, but the most important ones aren't those taking place at the FCC but in the marketplace. Our job is to write and administer the fairest and least burdensome rules we can, and otherwise stay as much as possible out of the way.

Let us know how we can help your industry. You are competitive. You are innovative. You have energy and optimism. And I hope the FCC will continue to be able to say that we have helped to promote -- or at least have not impeded -- this competition and innovation.

Thank you very much.