

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)
)
Telecommunications Relay Services and)
Speech-to-Speech Services for) CG Docket No. 03-123
Individuals with Hearing and Speech)
Disabilities)

COMMENTS OF SORENSON COMMUNICATIONS, INC.

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Attachments

- Appendix A: “The History of American Sign Language and the Demographics of Those Who Use It as Their Primary Language”

- Attachment 1: Declaration of Dr. Michael D. Pelcovits (providing an economic analysis explaining why price cap regulation is superior to cost-of-service regulation for VRS and IP Relay service)

- Attachment 2: Declaration of Commissioner Cheryl L. Parrino (based on her experience as a state regulator, explaining why price cap regulation is superior to cost-of-service regulation for VRS, describing the problems caused by the current rate methodology, and explaining why certain proposals would exacerbate those problems)

- Attachment 3: Declaration of Dr. John H. Johnson (providing an economic analysis of the labor market for interpreters)

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Sorenson Communications, Inc. (“Sorenson”) proposes herein a rate methodology that would accomplish the two principal goals of this proceeding: providing Video Relay Service (“VRS”) to all deaf Americans who want and need it, and making sure that VRS providers provide their unique and vital service as efficiently as possible. The proposed methodology is the same that this Commission wisely adopted in the Reagan-Bush era for local exchange carriers (“LECs”): a price cap approach. Specifically, the Commission should adopt price caps for both VRS and IP Relay, continuing the current approach of having a unified rate for the whole industry, including existing firms and new entrants. That price cap approach should remain in place for a minimum of three years. Applying a price cap methodology to all VRS firms would help stave off the looming interpreter shortage that today threatens the provision of VRS, which is a highly labor-intensive business; if this shortage is allowed to worsen, it eventually will lead to lower quality of service (including increased hold times) and higher costs. A price cap methodology would also create stronger market-based incentives to achieve efficiency; fairly compensate firms for providing VRS to those who have a legal right to have it; and

simplify the regulatory process while at the same time allowing the FCC to provide thorough and responsible oversight. Given the inherent benefits of price caps, a cost-of-service approach to setting rates for VRS and IP Relay is not the preferred option, and would require modification of the current methodology in a number of ways. Even with a corrected cost-of-service system, the current one-year rate period should be extended to a three-year period, so as to create incentives for firms to expand the interpreter labor pool and thereby forestall runaway cost increases.¹

I. INTRODUCTION AND SUMMARY

Sorenson addresses below all of the issues raised in the *Further Notice* to the extent they are relevant to the two Internet-based forms of Telecommunications Relay Services (“TRS”): VRS and Internet Protocol (“IP”) Relay. Those issues implicate three overarching questions: (i) How can the FCC meet the mandates of the Americans with Disabilities Act (“ADA”)? (ii) How can the FCC assure efficiency in paying for TRS?; and (iii) Is the best, most efficient way to cure the woeful access of the deaf to VRS (a penetration rate of only about 10 percent) to use a highly intrusive regulatory system akin to approaches rejected in the Reagan-Bush era?

The ADA includes two critical statutory mandates: (i) all deaf, hard-of-hearing, and speech-disabled Americans must have access to Relay services, and (ii) those services must be made available “in the most efficient manner.”² Today, those mandates

¹ See *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Further Notice of Proposed Rulemaking, 21 FCC Rcd 8379, ¶¶ 23, 30-31 (2006) (FCC 06-106) (“*Further Notice*”) (seeking comment on whether to adopt a rate period for VRS and IP Relay that is longer than the existing one-year period).

² 47 U.S.C. §§ 225(b)(1). Although more can and should be done to further the statutory demands for “functional equivalency” and “improved technology,” 47 U.S.C.

remain woefully unfulfilled. As noted, for example, only approximately 10 percent of deaf ASL users in the United States currently have access to VRS, the first and only technology that allows ASL users to communicate “by wire or radio” in their own language.³ By contrast, even the most underserved portion of the hearing population (Native Americans) has a telephone penetration rate that is more than *four times* the paltry penetration of VRS in the deaf ASL community.⁴ The approximately 90 percent of deaf ASL users without access to VRS are deprived of the means to use their own language to communicate from home to police if intruders threaten, to emergency medical services if injured or dangerously ill, to potential employers to seek work, or to friends or family. As the E911 Stakeholder Council has explained, it is critically important that VRS users be able to use their habitual communications devices during an emergency.⁵ “[P]eople rarely think clearly during an emergency,”⁶ and deaf VRS users cannot be expected to use a completely different mode of communication when an emergency arises.

As the Commission has recognized, the disparity between the universal availability mandated by the statute and the anemic access achieved to date should not

§§ 225(a)(3) & (d)(2), the advent of VRS and IP Relay – technologically advanced forms of TRS that afford unrivaled functional equivalence – has done much to advance those two important goals.

³ 47 U.S.C. § 225(a)(3).

⁴ App. A at 8.

⁵ Letter from E9-1-1 National Council of Stakeholders Of By & For Persons with Hearing and Speech Disabilities to Chairman Kevin J. Martin, FCC (Sept. 5, 2006) (filed in CG Docket No. 03-123 by Sherri Farinha Mutti, NorCal Center on Deafness, Oct. 5, 2006). (Unless otherwise indicated, all *ex parte* letters and comments cited herein are filed in CG Docket No. 03-123.)

⁶ *Id.* at 3 (page labeled 5).

and cannot persist. In fact, all five Commissioners have endorsed the goal of increasing the availability of TRS in general, and VRS in particular. As Chairman Martin exhorted in a separate statement issued with the *Further Notice*, the FCC should view this proceeding as an opportunity to “fulfill[] [the] statutory goal of ensuring that every person has equal access to this nation’s communications services.”⁷ Other Commissioners have expressed similar sentiments, by, for example: urging the FCC to “ensure that our [TRS] programs can be more widely used and consumer friendly”;⁸ recognizing the need to “increas[e] and improv[e] services to those with hearing and speech disabilities”⁹ and to “ensur[e] that every person who is deaf or hard of hearing will have access to a dial tone and the critical link to the rest of the world”;¹⁰ and expressing dismay that “there are still people who just don’t know about [VRS].”¹¹

Under these circumstances, the FCC must ensure that any new rate methodology advances the twin goals of universal availability and maximum efficiency, while remaining otherwise lawful and consistent with the public interest. Any new rate methodology also should not derail the progress that has to date been achieved. For example, the VRS and IP Relay industries are now characterized by robust competition from multiple firms, new entry, new technology, and (with respect to VRS) rapid progress to provide ASL users with access to VRS. The FCC also wisely kept the VRS

⁷ *Further Notice* at 31, Statement of Chairman Kevin J. Martin.

⁸ *Id.* at 35, Statement of Commissioner Deborah Taylor Tate.

⁹ *Id.* at 36, Statement of Commissioner Robert M. McDowell .

¹⁰ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Declaratory Ruling and Further Notice of Proposed Rulemaking, 21 FCC Rcd 5442, at 34 (2006) (FCC 06-57) (“*Interoperability Order*”), Statement of Commissioner Jonathan S. Adelstein.

¹¹ *Further Notice* at 33, Statement of Commissioner Michael J. Copps.

rate constant for the past two rate years, thereby helping to establish an expectation of rate stability that encourages providers to implement longer-term, more efficient business plans and reach out to new users. In a few years – perhaps as little as three or four – competitive forces and technological advances may result in most deaf and hard-of-hearing Americans finally gaining access to VRS and IP Relay. At that point, the VRS and IP Relay industries will have matured, and it is quite possible that by then all deaf Americans who want VRS will have access to it.

The ability of VRS and IP Relay providers to reach this maturation point depends on the FCC's establishing a compensation methodology that provides a stable and predictable level of funding that is sufficient to encourage providers to offer better service at a lower cost to greater numbers of deaf and hard-of-hearing users, in accord with the statutory mandate. The best way to achieve this goal is to adopt a "price cap" methodology that creates greater incentives for efficient provision of VRS and IP Relay and that ensures rate stability for at least three years. A price cap methodology is inherently superior to the current cost-of-service methodology because price caps align the incentives of providers with the public interest. If the Commission were to keep a cost-of-service approach, however, it would have to modify substantially the existing methodology. Under either alternative, the Commission must establish VRS and IP Relay rates that remain stable and predictable for a minimum of three years.

One of the most significant considerations in adopting a permanent rate methodology is the need to forestall a looming shortage of VRS interpreters. The provision of VRS is a highly labor-intensive endeavor, whose chief labor input (interpreters) is already in relatively short supply. As described in the attached

declaration of Dr. John Johnson, increasing demand for VRS combined with constraints on the supply of new interpreters is likely to lead to a shortage of interpreters and increases in wages, unless action is taken to expand the supply of qualified VRS interpreters. The Commission can stave off an interpreter shortage by promptly adopting a price cap methodology. A price cap approach would encourage providers to invest more aggressively in recruiting and training interpreters, and thereby keep down their labor costs and maintain an appropriate level of service quality. If the Commission were to revise the existing cost-of-service approach, it would need to make modifications, including allowing providers more fully to recover costs associated with the recruitment and training of interpreters, and extending the rate period to three years. If the Commission, through inaction or delay, allows the looming interpreter shortage to become a full-blown crisis, not only will quality of service worsen and costs rise, but the Commission may lose its ability to correct the underlying labor problem. Such a shortage also would create painful repercussions in the broader deaf community and run afoul of various statutes requiring community interpreters to be available in particular circumstances. For example, inaction by the Commission could impair the ability of members of the deaf community to receive adequate medical care, attend religious ceremonies, partake in legal proceedings, and participate in educational and training activities as the availability of interpreters dwindles and the cost of obtaining interpreting services increases.

As explained in detail below and in the attached declarations of Dr. Michael Pelcovits and Commissioner Cheryl Parrino, a price cap-based regime – one that establishes clear rules governing annual adjustments to VRS and IP Relay rates and

prescribes initial VRS and IP Relay rates at today's levels – would rectify the major shortcomings in the current scheme and provide a number of benefits, including the following:

- Creating stronger incentives for providers to improve the efficiency of their operations and thereby lower costs.¹²
- Keeping rates sufficiently stable, for a minimum of three years, to provide firms with enough predictability to make long-term investments and allocate money to programs that will reduce costs in the future (such as hiring and training more interpreters as a means of keeping labor costs low).¹³
- Simplifying the ratemaking process, which has been perennially complex, thus reducing the expenditure of time and money by firms, NECA, and the FCC on that process.

The FCC should not move to a more intrusive regulatory approach because it would consume resources, create disincentives to efficiency, and squelch competition among VRS and IP Relay providers. The Commission wisely rejected this approach more than twenty years ago; any “recidivist” flashback to the 1970s style of intrusive regulation would be inconsistent with the deregulatory approach embraced worldwide, including by this Commission. As Chairman Martin recently told Congress, the Commission should strive to eliminate counterproductive economic strictures that hinder

¹² As explained below, because the Commission has adopted a single rate for VRS and IP Relay services (based on the costs incurred by a hypothetical reasonably efficient provider), providers have a modest incentive to improve their efficiency. That incentive is blunted, however, because the current methodology ties rates to costs. A price cap regime would greatly enhance providers' incentive to pursue cost-saving efficiencies.

¹³ Interpreter costs are a very large part of the cost of providers' services. A price cap regime aligns incentives of providers with those of contributors by encouraging providers to recruit, retain, and train interpreters to keep labor rates down.

competition and innovation, but retain those rules needed to protect consumers and achieve broader social goals.¹⁴

As explained above, the chief policy goal in this proceeding is to establish a new rate methodology that furthers the statutory mandates of greater access and more efficiency. The cost-of-service methodology currently used by the FCC provides only limited incentives for providers to pursue these goals, and creates additional problems such as unstable rates and high administrative burdens. If, notwithstanding these problems, the Commission were to decide to retain a cost-of-service approach, it would have to adopt and implement several significant modifications, including: creating “accounts” that are better aligned with the costs actually incurred by providers; providing clearer guidance as to what costs are to be reported in each account; allowing providers to retain a reasonable profit; allowing providers to receive reimbursement for their research and development costs, as well as costs related to interpreter training and new user installations and training; and adopting a longer rate period. Although such modifications would improve the existing methodology, they would add to the already significant regulatory burdens inherent in that approach. Moreover, because providers’ incentives still would not be aligned with the public interest, VRS and IP Relay rates likely would be higher in the long run under any revised cost-of-service methodology.

If the FCC were nonetheless to retain a cost-of-service methodology instead of adopting a price cap regime, a particularly unwise step would be to adopt a so-called “true-up” scheme or to implement a post-hoc clawback of earned money from VRS and

¹⁴ Written Statement of the Honorable Kevin J. Martin Before the Committee on Commerce, Science & Transportation, U.S. Senate, at 2 (Sept. 12, 2006), *available at*: <http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-267390A1.pdf>.

IP Relay providers.¹⁵ In competitive markets, this sort of after-the-fact lowering, in effect, of the promised rate would discourage the most efficient firms from seeking to win the most users and to outperform their rivals. If providers knew that outperforming firms would be singled out for financial punishment, they would have no incentive to achieve greater efficiency gains than their rivals. Even in the context of regulating a monopoly provider under a cost-of-service or price cap system, a true-up encourages higher costs and discourages the pursuit of efficiency through investment in innovation. But in the context of a competitive market where new entry is easy – such as the VRS market – a so-called “true-up” discourages competition. Since VRS providers would receive no benefit from efforts to lower costs, every provider would increase costs or at least tolerate their increase; the VRS portion of the Interstate Telecommunications Relay Services Fund (“Fund”), in turn, would be larger than in the absence of a true-up. This bizarre and unfortunate outcome would harm contributors and deaf users alike, since the increased costs incurred under the misguided true-up scheme likely would not necessarily be accompanied by any improvement in quality of service or customer care. Similarly, setting rates based on each provider’s actual historic costs would have a high likelihood of resulting in unfair treatment of providers, would discourage providers from operating efficiently, and would not reduce administrative burdens.¹⁶

The Commission also should not set the VRS rate based on the lowest rate submitted in an auction.¹⁷ Adopting this approach of picking a winner rather than a rate would destroy the competition that has allowed VRS to grow and would have disastrous

¹⁵ See *Further Notice* ¶ 29.

¹⁶ *Id.*

¹⁷ *Id.* ¶ 28.

consequences for VRS users. For example, since most bidders could not afford to sit idle or offer VRS at the lowest bid rate, an auction scheme, if adopted, would inevitably cause a mass exodus from the VRS business, leaving only one or a few surviving VRS providers. Since, at the next auction, there would be few if any competing bidders, the survivors would raise the bid rate to a much higher level, confident that they could effectively block new entrants by exploiting their control of the interpreter labor pool, as well as any network advantages. In the long run, therefore, all the benefits of marketplace competition – innovation, efficiency, higher service quality, expanded availability, and the emergence of low-cost VRS providers as market leaders – would be lost under an auction scheme. Furthermore, even in the first auction, there is no sound basis for assuming that the winner would bid less than the rate set today.¹⁸ Instead, the winner would likely be the firm that can bid on providing service to all users – in effect, the winner would be a monopolist-in-the-making, and would secure its monopoly by a contract awarded by the government. This perverse result would, like any monopoly grant, produce higher costs rather than efficiency. Moreover, with the monopoly in hand, the winning bidder would not have any incentive to spend money on providing a high quality of service, but instead would have incentives to shortchange users.

II. THE FCC MUST ENSURE THAT THE STATUTORY MANDATE OF THE ADA IS FULFILLED

In assessing the relative merits of different rate methodologies in this proceeding, the Commission's touchstone should be the express directives of the ADA. In that

¹⁸ See Rebecca Smith, "Energy Auction in Illinois Will Lead to Jump in Rates for Consumers," WALL STREET JOURNAL, Sept. 18, 2006, at A6 ("Many Illinois consumers face power-rate increases of 22% to 55% in January as a result of the first energy auction conducted by state officials.").

landmark civil rights statute, Congress sought to “eliminat[e] discrimination against persons with disabilities in nearly all facets of society, including access to the telephone system.”¹⁹ Recognizing that the lack of telephone access for deaf, hard-of-hearing, and speech-disabled persons – a community of over 30 million people²⁰ – relegated them to “second-class citizenship,”²¹ the ADA added section 225 of the Communications Act, requiring Relay services to be made available to all such persons in the United States. By enacting this requirement, Congress sought to enable deaf, hard-of-hearing, and speech-disabled individuals to use the telephone to communicate with “anyone, anywhere, anytime,”²² and thereby participate in “the economic and social mainstream of American life.”²³ To achieve these goals, Congress directed the Commission to carry out a number of statutory duties, the most significant of which are discussed below.

¹⁹ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Report and Order, Order on Reconsideration, and Further Notice of Proposed Rulemaking, 19 FCC Rcd 12475, ¶ 3 n.17 (2004) (“*2004 Report and Order*”).

²⁰ Estimates of the size of this community vary widely, depending on how the relevant population is defined. Compare, e.g., David Noonan, “A Little Bit Louder, Please,” *NEWSWEEK*, June 6, 2005, at 42 (“More than 28 million Americans have some degree of hearing loss”), and *Telecommunications Relay Services, the Americans with Disabilities Act of 1990, and the Telecommunications Act of 1996*, Notice of Inquiry, 12 FCC Rcd 1152, ¶ 2 (1997) (“over 30 million Americans [have] hearing and speech disabilities”), with U.S. Census Bureau, “Americans with Disabilities: 2002,” Tables 2 & 7 (May 2006), available at: <<http://www.census.gov/hhes/www/disability/sipp/disable02.html>> (as of 2002, within the non-institutionalized civilian population of the United States, more than 8 million individuals had difficulty hearing a normal conversation, and more than 3.4 million individuals had difficulty having their speech understood by others).

²¹ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Order on Reconsideration, 20 FCC Rcd 13140, ¶ 24 (2005) (“*Spanish-ASL Order*”).

²² 135 Cong. Rec. S 10719 (Sept. 7, 1989) (statement of Sen. McCain).

²³ House Rept. 101-485, Part 2, at 129 (May 15, 1990) (“House Rept. 101-485 Pt. 2”); see also 136 Cong. Rec. S 9684 (July 13, 1990) (statement of Sen. Inouye).

A. The Commission Must Ensure that the Key Goals of Section 225 Are Effectuated

As described more fully below, section 225 requires the Commission to “ensure” that all deaf, hard-of-hearing, and speech-disabled individuals have (i) nationwide access, “to the extent possible,”²⁴ (ii) to “functionally equivalent” Relay services²⁵ (iii) that are made available “in the most efficient manner,”²⁶ (iv) pursuant to FCC rules that permit “the development of improved technology.”²⁷

Nationwide access. As its legislative history confirms,²⁸ section 225 is the logical extension of Congress’s long-standing goal of achieving universal service for all Americans.²⁹ Indeed, Section 225(b)(1) expressly incorporates by reference the goal of universal service codified in section 1 of the Communications Act:

In order to carry out the purposes established under section 1, . . . the Commission shall ensure that . . . telecommunications relay services are available, to the extent possible and in the most efficient manner, to hearing-impaired and speech-impaired individuals in the United States.³⁰

²⁴ 47 U.S.C. § 225(b)(1).

²⁵ *Id.* § 225(a)(3).

²⁶ *Id.* § 225(b)(1).

²⁷ *Id.* § 225(d)(2).

²⁸ *See, e.g.*, House Rept. 101-485 Pt. 2 at 129 (“Title IV . . . will help to further the statutory goals of universal service as mandated in the Communications Act of 1934”); *id.* at 130 (FCC should “ensure universal service to the hearing- and speech-impaired community,” and establishing minimum standards for TRS will help “attain[] meaningful universal service for this population”).

²⁹ *See* Section 1 of the Act, 47 U.S.C. § 151 (FCC shall “make available, so far as possible, to all the people of the United States . . . a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges”).

³⁰ 47 U.S.C. § 225(b)(1).

As the FCC has found, this directive must be construed broadly and literally.³¹ For example, the Commission must “evaluate the state of technology available to provide relay services, and determine what is possible.”³² If the Commission concludes that a particular form of TRS is possible, it must act to make that service available “nationwide” to all deaf, hard-of-hearing, and speech-disabled Americans.³³

Functional equivalency. Section 225 requires the Commission to ensure that Relay services are “functionally equivalent” to the phone services offered to hearing persons.³⁴ Congress imposed this requirement to “bridge the gap between the communications-impaired telephone user and the community at large,” emphasizing that to “participate actively in society, one must have the ability to call friends, family, businesses and employers.”³⁵ As the Commission has found, functional equivalence is

³¹ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Report and Order and Further Notice of Proposed Rulemaking, 15 FCC Rcd 5140, ¶¶ 89-90 (2000) (“*Improved TRS R&O*”).

³² *Id.* ¶ 91.

³³ *See, e.g., Id.* ¶ 18 (“We believe that nationwide availability of STS is possible, and we are therefore obligated to require it.”). The full *availability* of TRS should not be confused with full *usage*. Although the Commission is statutorily obligated to adopt a pricing regime that promotes the former goal, it is under no corresponding obligation to promote the latter. The Commission therefore does not need to attempt to maximize minutes of use for VRS or IP Relay, either on a per-user basis or in the aggregate. Nor should the Commission expect that usage of those services will increase in direct proportion to any increase in the services’ availability. In fact, making VRS fully available to all deaf ASL users will not result in the entire community actually using VRS. To the contrary, it is likely that many ASL users will either opt not to use VRS at all or use it only infrequently (*e.g.*, for special occasions).

³⁴ 47 U.S.C. § 225(a)(3) (defining TRS as “telephone transmission services that provide the ability for an individual who has a hearing impairment or speech impairment to engage in communication by wire or radio with a hearing individual in a manner that is functionally equivalent to the ability of an individual who does not have a hearing impairment or speech impairment to communicate using voice communication services by wire or radio.”).

³⁵ House Rept. 101-485 Pt. 2 at 130.

not a static concept, but rather “requires periodic reassessment” in light of the “ever-increasing availability of new services and the development of new technologies,” such as VRS.³⁶

In the most efficient manner. As noted, section 225 requires the Commission to ensure that Relay services are made available, “to the extent possible and in the most efficient manner,” to all deaf, hard-of-hearing, and speech-disabled Americans.³⁷ In the case of VRS and IP Relay, the Commission wisely has chosen to advance the goals of universal access and efficiency by adopting rules that encourage multiple providers to compete for potential users, and reimbursing all providers at a single per-minute rate designed to allow a hypothetical reasonably efficient provider to recover its costs. This approach is good for consumers because it enables VRS and IP Relay users today to have a choice among several providers. In addition, the use of a single rate provides an incentive to become more efficient than the hypothetical “reasonable” provider. If it is to meet its statutory obligations, however, the FCC must strengthen incentives to provide service in the most efficient manner, and ensure that its regulations “neither unduly raise the costs of providing TRS, nor displace market forces that could improve TRS services.”³⁸

Improved technology. In adopting section 225, Congress sought to encourage the use of “state-of-the-art technology” and guard against “freezing technology or thwarting

³⁶ *Improved TRS R&O* ¶ 4.

³⁷ 47 U.S.C. § 225(b)(1).

³⁸ *Telecommunications Relay Services, the Americans with Disabilities Act of 1990, and the Telecommunications Act of 1996*, Notice of Inquiry, 12 FCC Rcd 1152, ¶ 23 (1997).

the introduction of a superior or more efficient technology.”³⁹ Congress therefore directed the Commission to ensure that its regulations implementing section 225 “encourage, consistent with section 7(a) of this Act,⁴⁰ the use of existing technology and do not discourage or impair the development of improved technology.”⁴¹

Implications for VRS. VRS has been and remains the only form of TRS that permits users of ASL to communicate in their own language. Typically, a VRS call is initiated when a deaf person establishes a video link, via a broadband Internet connection, with a VRS interpreter.⁴² The interpreter, in turn, places an outbound telephone call to a hearing person. During the call, the interpreter communicates in ASL with the deaf person and by voice with the hearing person.⁴³ As a result, the conversation between the two parties flows with a rapidity, nuance, and fluency that rivals that of spoken English and that is “unimaginable” with other forms of TRS.⁴⁴ ASL users who communicate via VRS thus enjoy the greatest degree of functional equivalency available today – a fact the

³⁹ House Rept. 101-485 Pt. 2 at 131, 133-34.

⁴⁰ Section 7(a) of the Communications Act states: “It shall be the policy of the United States to encourage the provision of new technologies and services to the public. Any person or party (other than the Commission) who opposes a new technology or service proposed to be permitted under this Act shall have the burden to demonstrate that such proposal is inconsistent with the public interest.” 47 U.S.C. § 157(a).

⁴¹ 47 U.S.C. § 225(d)(2).

⁴² VRS calls can also be initiated by hearing individuals who call a VRS provider over the telephone. The interpreter then establishes a video link to the deaf person.

⁴³ Although VRS, like all forms of TRS, must be made available to individuals who are hard-of-hearing or speech-disabled, the vast majority of VRS users are deaf.

⁴⁴ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Report and Order, 20 FCC Rcd 13165, ¶ 3 (2005) (“*Speed-of-Answer Order*”).

Commission has repeatedly emphasized.⁴⁵ Accordingly, section 225 requires the Commission to make VRS available nationwide, “to the extent possible and in the most efficient manner,” to all deaf ASL users.⁴⁶ Today, this community of potential VRS users most likely numbers in the hundreds of thousands.⁴⁷ Making VRS available to all such individuals is of the utmost importance and should be a key goal of this proceeding.

B. Title IV Is Directed at Universal Service, Not Accommodation

The *Further Notice* suggests that TRS is an “accommodation” under the ADA, and that providers of TRS are therefore not entitled to receive a reasonable profit or to be

⁴⁵ See, e.g., *id.*; *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Order, 21 FCC Rcd 6733, ¶ 4 (2006) (FCC 06-81); *Interoperability Order* ¶ 11; *Spanish-ASL Order* ¶ 3. As explained below, IP Relay is the most functionally equivalent form of text-based TRS available today.

⁴⁶ 47 U.S.C. §§ 225(a)(3), (b)(1), & (d)(2); see discussion *supra* at 2-4.

⁴⁷ Although there is no recent data that is reliable, the number of deaf ASL users in 1972 likely fell within a range of 277,000 to 375,000. Ross E. Mitchell, Travis A. Young, Bellamie Bachleda, Michael A. Karchmer, “How Many People Use ASL in the United States? Why Estimates Need Updating,” *Sign Language Studies* 6:3 (2006): 306-335, at 322, 329; *Can you tell me how many deaf people there are in the United States?*, Gallaudet Research Institute (“GRI”) website, Demographics section, available at: <<http://gri.gallaudet.edu/Demographics/deaf-US.php>>. GRI estimates that “if the proportion of deaf signers has remained roughly the same, then they would continue to number in the hundreds of thousands today (360,000 to 517,000).” *Id.* A U.S. Census Bureau survey conducted in 2002 estimates that approximately 7.8 million Americans 15 years of age and older had difficulty hearing a normal conversation, including approximately 1 million who reported being “unable to hear” or had severe difficulty hearing a conversation. Erika Steinmetz, *Current Population Reports in Americans With Disabilities: 2002, Household Economic Studies*, U.S. Census Bureau, Table A (issued May 2006), available at: <<http://www.census.gov/prod/2006pubs/p70-107.pdf>>. It is unclear, however, whether the latter group was limited to deaf individuals, or also included hard-of-hearing persons. Compare *id.* (972,000 individuals unable to hear), with *id.* at Table 2, *supra* note 20 (972,000 individuals with severe difficulty hearing conversation).

reimbursed for certain costs incurred in the provision of TRS.⁴⁸ Both the premise and the reasoning are wrong, however: TRS is not an “accommodation,” and, even if it were, that would not preclude providers from earning a reasonable profit.

The purpose of the ADA is to eliminate discrimination against individuals with disabilities in four distinct areas, each of which is addressed in a separate statutory Title: employment (Title I),⁴⁹ public services (Title II),⁵⁰ public accommodations (Title III),⁵¹ and telecommunications (Title IV).⁵² Although Titles I - III mandate certain “accommodations,”⁵³ Title IV does not. In fact, the word “accommodation” does not even appear in Title IV, even though it is used dozens of times in the preceding titles.

As explained above, both the express language of section 225 and its legislative history confirm that the purpose of Title IV (and hence TRS) is not to provide an “accommodation,” but “to ensure universal service to the hearing- and speech-impaired community.”⁵⁴ Thus, section 225 is more analogous to sections 1 and 254 of the

⁴⁸ *Further Notice* ¶ 8 (“[W]e are mindful of the role of TRS as an accommodation under the ADA for persons with disabilities”); *see also id.* ¶ 28.

⁴⁹ 42 U.S.C. §§ 12111-12117.

⁵⁰ *Id.* §§ 12131-12165.

⁵¹ *Id.* §§ 12181-12189.

⁵² 47 U.S.C. § 225. A fifth title of the ADA assembles various “miscellaneous” provisions. 42 U.S.C. §§ 12201-12213.

⁵³ Titles I and II require private and public entities, respectively, to make “reasonable accommodations” with respect to their employees. *See* Shaller, “‘Reasonable accommodation’ under the Americans with Disabilities Act – what does it mean?” 16 *Empl. Rel. L.J.* 431, Spring 1991; DOJ Title II Manual II-4.3200. As noted, Title III regulates public “accommodations” in various ways. Neither type of “accommodation” has relevance to TRS provided under Title IV.

⁵⁴ House Rept. 101-485 Pt. 2 at 130; *see also* 47 U.S.C. § 225(b)(1) (incorporating by reference the universal service mandate of section 1 of the Act).

Communications Act than to Titles I-III of the ADA.⁵⁵ Although Congress intended section 225 and other provisions of Title IV to be *consistent* with the goals enshrined in Titles I-III,⁵⁶ it did not intend for the Commission's central duty under Title IV – ensuring that deaf, hard-of-hearing, and speech-disabled individuals have universal access to communications services – to be diluted by or confused with provisions set forth in other Titles of the ADA.⁵⁷ The Commission therefore may not use provisions in Titles I - III to reduce the universal access mandate of section 225 to a mere “accommodation” requirement. Indeed, TRS involves the creation of entirely new services, many of which have been developed using new technologies. The FCC's mandate under section 225 is to ensure that there is universal access to these new and innovative services.⁵⁸

Even if the FCC were correct in labeling TRS as an “accommodation,” there would be neither legal nor logical support for the denial of a reasonable profit to TRS providers. In fact, denying providers a reasonable profit would create disincentives for new providers to enter the TRS business or for existing providers to stay in the business, let alone innovate or expand the availability of service to additional users. This result would be contrary to the clear statutory mandate to make TRS available “to the extent

⁵⁵ Indeed, as noted, section 1 is explicitly incorporated by reference into section 225.

⁵⁶ See House Rept. 101-485 Pt. 2 at 131 (“By requiring telecommunications relay services to be provided throughout the United States, this section [Title IV] takes a major step towards enabling individuals with hearing and speech impairments to achieve the level of independence in employment, public accommodations and public service *sought by other sections* of the Americans with Disabilities Act.”) (emphasis added).

⁵⁷ Compare 42 U.S.C. §§ 12111-12117, 12131-12165, (focusing on accommodation), with 47 U.S.C. § 225 (focusing on universal service).

⁵⁸ 47 U.S.C. § 225(b)(1).

possible” throughout the country and to encourage the use of existing technologies and “not discourage or impair the development of improved technology.”⁵⁹

III. VRS AND IP RELAY ARE UNIQUELY SUITED TO ADVANCE THE ADA’S MANDATES

A. The Enormous Potential of VRS and IP Relay Is Currently Thwarted by the Lack of Access to Those Services

Throughout history, deaf people have experienced discrimination in all walks of life. Before the twentieth century, the deaf were often considered unintelligent or unable to be educated, and were forced to society’s fringes.⁶⁰ Notwithstanding a general lessening of ignorance and hostility in the late twentieth century, many deaf Americans continued to be – and, to this date remain – excluded from the employment opportunities, popular culture, and other dominant institutions of mainstream hearing society.⁶¹

Audism (discrimination against non-hearing individuals) is particularly acute for deaf persons whose primary language is ASL.⁶² “A uniquely expressive and powerful” visual language,⁶³ ASL is distinct from any spoken language: it maintains its own vocabulary, grammar, syntax, and cultural heritage, and conveys ideas in ways that differ from English.⁶⁴ Consequently, when a deaf person whose primary language is ASL must

⁵⁹ *Id.* §§ 225(b)(1) & (d)(2). Under the analogous universal service mandate of section 254 of the Act, for example, the Commission has permitted providers of supported services to earn a reasonable profit.

⁶⁰ *See* App. A at 1, 5.

⁶¹ *Id.* at 5-7 (noting, for example, that in 2002, the employment rate of persons with “severe difficulty hearing normal conversation” was about 18% lower than that of the U.S. population as a whole, and that employed deaf Americans earn about 25% less on average than the American population at large).

⁶² *Id.* at 7.

⁶³ Oliver Sacks, *Seeing Voices* at 20, Vintage Books (1989).

⁶⁴ App. A at 2.

communicate in English, he or she is communicating in a foreign language that lacks some of the basic components for expression found in his or her native language.⁶⁵

Because many hearing people do not appreciate the uniqueness of ASL or its profound importance to the deaf community and deaf identity, they often ignore or underemphasize the importance of facilitating the ability of deaf persons to communicate in their own language.⁶⁶

As explained above, Title IV of the ADA was designed to dismantle the barriers traditionally experienced by deaf individuals when attempting to communicate “by wire or radio” with hearing people.⁶⁷ For a full decade after the ADA’s passage, however, ASL users continued to lack any option to use their own language when using Relay services. Instead, deaf Relay users were effectively tethered to text telephones (“TTYs”), specialized devices connected via a dedicated link to the Public Switched Telephone Network (“PSTN”). Because TTYs permit deaf users to communicate only through the laborious process of manually typing outgoing portions of the conversation and then reading the incoming portions, TTYs are incapable of affording deaf ASL users the ability to use their own language when placing phone calls to family, friends, co-workers, and others – an ability long taken for granted by hearing people. So long as deaf ASL users were limited to TTYs, therefore, they were denied the most fundamental right to which they are entitled under the ADA – the opportunity to communicate by phone in a manner that is “functionally equivalent” to that enjoyed by hearing people.⁶⁸

⁶⁵ *Id.*

⁶⁶ *Id.* at 2-5.

⁶⁷ 47 U.S.C. § 225(a)(3).

⁶⁸ *Id.*

This injustice began to be rectified only in 2000, when the Commission recognized VRS as a form of TRS.⁶⁹ As the first and only Relay technology that allows deaf ASL users to communicate in their own language, VRS has had a revolutionary impact on the lives of tens of thousands of deaf Americans. For the first time, deaf ASL users have been able to harness state-of-the-art Internet and video technology to communicate by phone with a rapidity, fluency, and nuance that rivals that of traditional hearing-to-hearing calls.⁷⁰ And, for the first time, friends, family, and co-workers have been able to experience deaf ASL users expressing themselves naturally and fully, unconstrained by the inherent limitations of TTYs. As borne out by over three thousand post cards, letters, and emails sent to the FCC by deaf people in recent months, the advent of VRS has dramatically improved the lives of those ASL users who are aware of the service and have access to it, permitting them, in the words of one person, to “reach out to my doctor or pharmacist, to seek legal help, or to inquire about items that are out or on sale, as well as [to engage in] everyday communication with my family and friends.”⁷¹

⁶⁹ *Improved TRS R&O* ¶¶ 22-24. VRS was initially developed in the 1990s, largely through the pioneering efforts of Ed Bosson. North Carolina was the first state to officially approve VRS for use, but Texas was the first to purchase statewide services from Sprint and Communications Service for the Deaf (“CSD”) in 1998. Karen Peltz Strauss, *A New Civil Right* at 133, Gallaudet University Press (2006) (“Strauss, *A New Civil Right*”).

⁷⁰ VRS therefore satisfies both the functional equivalency mandate of the ADA, and that statute’s “improved technology” requirement. *See, e.g., VRS Interoperability Order*, ¶ 11 (VRS “provides a degree of ‘functional equivalency’ that is not attainable with text-based TRS”); *see also* Strauss, *A New Civil Right* at 133 (describing ways in which VRS “offered a vast improvement over text-based relay services for people who used sign language as their primary or preferred language”).

⁷¹ Letter from Vikee Waltrip (May 26, 2006); *see also, e.g.,* letter from Mary Moore (Board President of Central Florida Deaf Services) (May 18, 2006) (filed May 19, 2006, in letters from “Various”) (stating that she has seen an increase in the number of clients who have trouble using TTY but who use VRS “with ease as they can communicate in their native language . . . with their doctors, businesses, their employers, friends, and

The advent of IP Relay has had a similar (if less revolutionary) impact on the lives of deaf and hard-of-hearing individuals who place text-based Relay calls. With the approval of IP Relay as a form of TRS in 2002,⁷² users were freed to make text-based Relay calls via the Internet using a computer, web phone, personal digital assistant, or many other IP-capable devices, rather than only a dedicated TTY. This allowed for increased mobility, since IP Relay can be used from any device with Internet access, including wireless devices such as Sidekicks and BlackBerrys. By harnessing the versatility, power, and ubiquity of the Internet, IP Relay has been able to provide users substantial benefits – “in quality and flexibility of service, in ease of use and convenience, and in the potential for additional service features in the future” – that could not be achieved with traditional TTY-based service.⁷³

families.”); letter from Sandralyn D. Bailey, CGB to Bill Caton, Deputy Secretary, FCC (July 7, 2006) (filed July 11, 2006, in letters from “Various”) (explaining that the CGB has received 3,360 comments, including some duplicates, and attaching three examples, each of which states that many deaf people, their families and coworkers depend on VRS, and that the FCC should encourage more people to use VRS); “Video Relay Service: FCC Consumer Facts,” available at: <<http://www.fcc.gov/cgb/consumerfacts/videorelay.html>> (listing the following benefits of VRS: allowing ASL users to communicate in their primary language instead of having to type what they want to say; allowing users “to more fully express themselves through facial expressions and body language, which cannot be expressed in text”; allowing calls to flow back and forth “just like a telephone conversation between two hearing persons”; allowing conversations to take place much more quickly than with text-based TRS; and allowing calls to be “made between ASL users and hearing persons speaking either English or Spanish”).

⁷² *Provision of Improved Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities; Petition for Clarification of WorldCom, Inc.*, Declaratory Ruling and Second Further Notice of Proposed Rulemaking, 17 FCC Rcd 7779, ¶ 1 (2002).

⁷³ *Id.* ¶ 7; see also “IP Relay Service: FCC Consumer Facts,” available at: <<http://www.fcc.gov/cgb/consumerfacts/iprelay.html>> (listing the following benefits of IP Relay: availability, convenience, multiple calls, quality, and multivendors); Strauss, *A New Civil Right* at 137 (describing benefits of IP Relay compared to TTYs).

Despite the enormous potential of VRS and IP Relay to improve the lives of deaf and hard-of-hearing people and fulfill the mandate of the ADA, many deaf and hard-of-hearing Americans are not aware of those services, do not understand their unique abilities, or do not otherwise have access to them. For example, only about ten percent of deaf ASL users currently have access to VRS. As a result, a shocking percentage of ASL users live without the opportunity to use their own language to call a friend or make an appointment at a doctor's office. In fact, deaf Americans who use ASL remain by far the most poorly served community in the United States in terms of access to communications services.⁷⁴ The Commission has a legal and moral obligation to end this unconscionable relic of audism by ensuring, as quickly as possible, that VRS is made available to all deaf ASL users.

B. The Potential of VRS Is Further Threatened by a Looming Interpreter Shortage

As explained in the Johnson and Pelcovits declarations, the provision of VRS is a highly labor-intensive endeavor whose chief labor input (interpreters) is in relatively short supply.⁷⁵ In fact, increasing demand for VRS combined with constraints on the supply of new interpreters is likely to lead to a shortage of interpreters and increases in wages, unless action is taken to expand the supply of qualified VRS interpreters.⁷⁶ Although the *Further Notice* correctly recognizes the labor-intensive nature of VRS and the importance of ensuring adequate compensation for interpreter costs,⁷⁷ it fails to

⁷⁴ See *supra* at 3; App. A at 7-8.

⁷⁵ Johnson Decl. ¶¶ 7-13, 23, 25; Pelcovits Decl. ¶¶ 10, 13.

⁷⁶ Johnson Decl. ¶ 25.

⁷⁷ *Further Notice* ¶ 25.

address the equally important need to expand the pool of interpreters and provide continuing education for existing interpreters.⁷⁸

The Commission can stave off an interpreter shortage by promptly adopting a price cap methodology. A long-term price cap would encourage providers to invest more aggressively in recruiting and training interpreters, and thereby keep down their labor costs while maintaining an appropriate level of service quality.⁷⁹ Under a cost-of-service approach, the Commission would have to make modifications to allow providers more fully to recover costs associated with the recruitment and training of interpreters, and extend the rate period to three years. If the Commission, through inaction or delay, allows the looming interpreter shortage to become a full-blown crisis, not only will quality of service worsen and costs rise, but the Commission may lose its ability to correct the underlying labor problem. Eventually, the interpreter shortage could become so severe that it could not be readily alleviated by additional money or effort. Such a shortage could create painful repercussions in the broader deaf community, including depleting the supply of interpreters available to work in-person in schools, doctors'

⁷⁸ See Pelcovits Decl. ¶¶ 13-16, 32; Parrino Decl. ¶¶ 19-25; Johnson Decl. ¶¶ 15, 18; see also Distance Opportunities for Interpreter Training Center, "Video Relay Services Interpreting Task Analysis Report" at 24 (Sept. 2005), available at: <<http://www.unco.edu/doit/articles/vrs%20task%20force%20report.pdf>> ("DOIT Report").

⁷⁹ See Johnson Decl. ¶ 18 ("VRS providers must begin investing now to increase available interpreting capacity in light of the expected increase in VRS demand. Otherwise, wages can be expected to rise, putting pressure on the per-minute reimbursement rate for VRS."); *id.* ¶ 15 ("unless and until new sources of VRS interpreting can be found or created, the labor cost per minute of interpreting can be expected to rise in the face of increasing demand").

offices, and other important venues. Any such depletion would run afoul of various statutes requiring community interpreters to be available in particular circumstances.⁸⁰

One of the primary causes of the looming interpreter shortage is VRS growth, which has put additional strain on an already limited supply of certified interpreters. As the number of VRS users continues to grow, more interpreters will be needed.⁸¹ The challenge facing the Commission is to give providers robust incentives – preferably through price caps – to create a larger, more efficient interpreter labor pool. It commonly takes 5-7 years for new interpreters to be trained and become qualified to be VRS interpreters.⁸² New interpreters will be needed not only to replace retiring interpreters, but also to meet increases in demand while, as noted, still providing the community

⁸⁰ See *id.* ¶ 18. Legal requirements to provide interpreters for the deaf are contained, *inter alia*, in the Rehabilitation Act of 1973, as amended, 29 U.S.C. §§ 701-797b (requiring “interpreter services provided by qualified personnel for individuals who are deaf or hard of hearing,” *id.* § 723); the Individuals with Disabilities Education Act (“IDEA”), 20 U.S.C. §§ 1400-1485; and the Americans with Disabilities Act, 42 U.S.C. §§ 12101-12213 (requiring an entity offering its services to the public to make available reasonable auxiliary aids and accommodations, such as providing a sign language interpreter, to ensure that any individual can “participate in or benefit from the goods, services, facilities, privileges, advantages, or accommodations of an entity,” 42 U.S.C. § 12182). See, e.g., *State ex rel. Lambert v. West Va. State Bd. of Educ.*, 191 W. Va. 700 (W. Va. 1994) (affirming deaf student’s right to a sign language interpreter to enable participation in school-sanctioned extracurricular activities, as well as the classroom); *Mayberry v. Von Valtier*, 843 F. Supp. 1160 (E.D. Mich. 1994) (finding evidence of discrimination when physician suggested that deaf patient should provide her own sign language interpreter); *Calloway v. Boro of Glassboro Dep’t of Police*, 89 F. Supp. 2d 543 (D. N.J. 2000) (finding that the provision of a qualified sign language interpreter is required in the context of a station-house investigative interview, and utilizing the services of a police officer who understood sign language but was not a certified interpreter is inadequate).

⁸¹ See Johnson Decl. ¶¶ 14-18. Ultimately, growth will be limited by the number of deaf ASL users interested in VRS.

⁸² See *id.* ¶ 7 (“becoming an effective VRS interpreter requires extensive training, even beyond the years of training required to be an ASL interpreter”); see also *id.* ¶¶ 8-13.

interpreting mandated by various statutes and demanded by the Deaf community.⁸³ Any VRS rate methodology therefore should provide adequate compensation for providers to recruit and train a sufficient number of new interpreters.

A rate methodology also should afford providers the financial means to provide continuing education to existing VRS interpreters. Even after they have been certified, interpreters need additional seasoning before they are ready to handle the difficult task of providing VRS.⁸⁴ Unlike traditional community interpreting, VRS requires interpreters to move quickly from one conversation to another. The burden imposed by such rapid transitions is exacerbated by the need for the VRS interpreter to adapt immediately to the unique demands of each conversation. VRS calls can be placed by and to persons located anywhere in the United States. As a result, on any day a VRS interpreter is likely to handle calls involving ASL users from different parts of the country, with widely varying “accents” or dialects and different levels of signing proficiency (including the potential for “home signs”), all without the background context usually afforded to “live” interpreters. These demands require special training and continuing education and professional development.⁸⁵ If VRS interpreters are not extremely proficient, the service will not provide the seamless, real-time communication demanded by the “functional equivalence” mandate of the statute. Adequate training of new and existing interpreters will also enhance the efficiency of interpreters, a goal the FCC has sought to promote.⁸⁶

⁸³ See *id.* ¶¶ 15-16.

⁸⁴ See *id.* ¶ 12.

⁸⁵ See *id.* ¶¶ 11-12, 25; DOIT Report at 5-6.

⁸⁶ See *Further Notice* ¶ 25.

IV. A PRICE CAP METHODOLOGY FOR VRS AND IP RELAY WOULD BEST ADVANCE THE GOALS CODIFIED IN SECTION 225 OF THE COMMUNICATIONS ACT

As explained above, section 225 directs the Commission to ensure that TRS is made available in a way that satisfies four primary goals: nationwide access; functional equivalency; maximum efficiency; and improved technology. Any rate methodology must be evaluated against these goals.

A rate methodology based on price caps is plainly superior to the existing methodology – as well as other approaches, such as competitive bidding – in advancing the goals codified in section 225. The incentives created by a price cap system emulate the incentives to innovate and lower costs that exist in a fully competitive marketplace. That is appropriate in this case because, although VRS and IP Relay are competitively provided, firms are not competing based on price, given the single-payer model adopted for TRS. By aligning the incentives of providers with the public interest, price caps encourage providers to offer the highest quality service to the greatest number of users in the most efficient manner. Providers, in short, are encouraged to fulfill all four of the principal goals codified in section 225.

The price cap methodology proposed herein would have three primary benefits: (1) a price cap would create incentives for all VRS and IP Relay providers to lower costs (including by recruiting new interpreters and training existing ones), whereas any cost-of-service approach creates incentives to allow reimbursable costs to go up; (2) a price cap for a minimum of three years would provide firms enough predictability to allocate money to programs that will reduce costs in the future (such as hiring and training more

interpreters so as to keep labor costs down);⁸⁷ and (3) a price cap would simplify the process and reduce the expenditure of time and money by firms, NECA, and the FCC in what has been a perennially complex process of rate setting.⁸⁸

The best way for the Commission to improve the current scheme of VRS and IP Relay rate regulation is to adopt a “price cap” methodology under which rates would be set at reasonable initial levels, subject to an annual adjustment for inflation and efficiency gains, as well as any adjustments needed to address changes in exogenous costs.⁸⁹ After at least three years, the Commission would review its price cap formulas and modify them to the extent necessary.

A. The FCC Has Used Price Cap Regulation to Create Incentives for Telephone Companies to Be More Efficient

Price cap regulation is a form of rate regulation introduced by the FCC in the late 1980s and applied initially to AT&T (at that time still dominant in the provision of long distance services) and subsequently to the largest local exchange carriers, including the Bell Operating Companies (“BOCs”). Prior to the introduction of price caps, the Commission had used a form of “cost-of-service” regulation to regulate the prices of AT&T and the local telephone companies. This particular type of cost-of-service

⁸⁷ See *Further Notice* ¶¶ 25, 27 (noting that “labor costs for VRS constitute[] a much higher proportion of overall costs than for other forms of TRS,” and seeking comment on how a new pricing regime could best encourage “the efficient utilization of labor” for VRS).

⁸⁸ See *id.* ¶ 7 (describing “administrative challenges” presented in recent years under the present rate methodology, particularly with respect to the VRS rate); *id.* ¶¶ 46-47 (seeking comment on how the Fund might be better and more efficiently administered).

⁸⁹ Although Sorenson proposes a rate regulation method based on existing price cap regulations, Sorenson’s proposal differs from traditional price cap regulation in several key aspects. See, e.g., note 95 *infra*. For the sake of convenience, however, Sorenson refers to its price cap-based proposal as a price cap methodology.

regulation was called “rate-of-return” regulation because it was designed to limit the return that a carrier could earn on its rate base, which is defined as the net book value of the investments used to provide interstate service.

The Commission concluded that a price cap regime would create a continuing incentive for regulated carriers to provide service more efficiently, which rate-of-return regulation did not.⁹⁰ Specifically, carriers under rate-of-return regulation were permitted to set rates that were designed to recover their forecasted costs in the upcoming year. If a carrier forecasted that it would provide service at a lower cost than the previous year, its rates were simply lowered to reflect the savings. Hence the regulated carrier obtained no benefit from the efficiency gain. Indeed, rate-of-return regulation actually creates a perverse incentive for a carrier to increase unnecessarily its investments in order to increase the base on which it is permitted to earn a return.⁹¹ A price cap regime, by contrast, uses a price index to limit the maximum prices that a carrier may charge. If a price cap carrier is able to reduce its costs of service, it is permitted to retain all or part of those savings, as long as its prices remain below the indexed maximum. In this regard, the incentives created by a price cap system are similar to the profit-maximizing incentives of a competitive marketplace.⁹² This is appropriate for VRS and IP Relay because although those services are provided competitively, there is a single payor (the Fund) and this distorts incentives and behavior compared to a truly competitive, but

⁹⁰ See *Policy and Rules Concerning Rates for Dominant Carriers*, Report and Order and Second Further Notice of Proposed Rulemaking, 4 FCC Rcd 2873, ¶¶ 14, 36, 41-43 (1989) (“*AT&T Price Cap Order*”); *Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd 6786, ¶¶ 1, 30-31, 35, 65 (1990) (“*LEC Price Cap Order*”).

⁹¹ See *AT&T Price Cap Order* ¶ 30.

⁹² See *id.* ¶ 36; *LEC Price Cap Order* ¶ 2.

unregulated market. The Commission also anticipated that price caps would produce savings in administrative costs, both for carriers and the Commission, by eliminating the need for the annual submission of detailed forecasts of costs, demand, and revenues to support a carrier's proposed rates for the upcoming rate year.⁹³

The form of price cap regulation applied to the telephone companies established the initial price cap indices ("PCIs") on the basis of each carrier's most recent cost-of-service rates. The PCIs were then adjusted annually in accordance with a formula prescribed by the Commission. The FCC's price cap formula for local telephone companies originally had three main components: (1) a measure of the previous year's inflation; (2) a measure that reflects the extent to which the annual productivity gains of the telephone industry are expected to exceed the annual productivity gains of the economy as a whole;⁹⁴ and (3) a provision for "exogenous" cost changes – principally changes in costs that are beyond the telephone company's control, such as a cost increase caused by a change in FCC regulations. In addition, the Commission provided for a performance review after the initial three years of operation under price caps.

B. A Price Cap Regime Is the Best Way of Advancing Congress's Goals

A price cap regime that establishes clear rules governing annual adjustments to the cap and prescribes initial VRS and IP Relay rates at the level that would compensate adequately a "reasonable" provider would rectify the major shortcomings in the current

⁹³ See *AT&T Price Cap Order* ¶ 107; *LEC Price Cap Order* ¶ 37.

⁹⁴ As discussed below, after the adoption of the *CALLS Order*, the X factor is no longer a productivity estimate. *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board On Universal Service*, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962, ¶ 40 (2000) ("*CALLS Order*").

scheme.⁹⁵ Specifically, such a system would give each provider a strong, ongoing incentive to provide service as efficiently as possible to ensure that its costs will be less than the permissible rate.⁹⁶ Competition plus a price cap is the ideal solution to advance the statutory goals of achieving expanded access to IP Relay and VRS and efficient provision of those services. Moreover, by making the annual rate adjustment more predictable, a price cap scheme will encourage providers to make short- and long-term investments that are likely to produce such efficiency gains.⁹⁷

For example, the costs associated with ASL interpreters are the single largest expense in the provision of VRS. As explained above, providers should have an incentive to ensure that the pool of available interpreters continues to grow so that there is an adequate supply to meet the increased demand for their services, both for VRS and in the community. Otherwise, a shortage in interpreters would cause the costs of interpreters to increase, potentially precipitously. A price cap regulatory regime would reinforce a VRS provider's incentive to keep its interpreter costs at reasonable levels, since the FCC would not allow the price index to rise because of an increase in those costs.⁹⁸ In addition, the stability and predictability of such a regime would encourage

⁹⁵ A price cap regime would differ from the FCC's scheme for local telephone companies in at least one very significant respect. A telephone company's price index limited the maximum prices that the company could charge for a variety of services that were subject to that index. A VRS index would limit the price that a provider could charge for a single service, VRS. The IP Relay index also would be applied to the rate for a single service. Consequently, the annual price cap adjustments discussed in these comments would be made directly to the VRS and IP Relay rates, rather than to the indices.

⁹⁶ See Pelcovits Decl. ¶¶ 31, 33-34, 37, 64-65.

⁹⁷ See *id.* ¶ 34.

⁹⁸ In contrast, a cost-of-service regime would create no incentive for providers to control interpreter costs, since any increase in costs would result in a corresponding

providers to make short-term as well as long-term investments that are designed to foster growth in the pool of ASL interpreters. In other words, a properly designed price cap regime would give VRS and IP Relay providers the same incentives to reduce costs and manage their service offerings efficiently that a competitive marketplace would provide.

A price cap regime similarly should give VRS and IP Relay providers a strong incentive to add new customers.⁹⁹ Under the statute, the Commission must ensure that deaf and hard-of-hearing individuals who could benefit from VRS or IP Relay are informed of the availability of those services, and can obtain access to them. The most efficient way to achieve this result is to ensure that providers have compelling incentives to expand the reach of their service by adding new customers. Under a price cap system that encourages providers to engage in well-planned business behavior, VRS providers will continue to compete with each other for new users. The combination of price cap regulation and interoperability would make it critical for providers to operate their businesses efficiently and in a user-friendly manner. Competition will also drive providers to grow their businesses by expanding access to VRS and IP Relay services for the deaf and hard-of-hearing community.

A price cap is a mechanism that can be used to drive costs down by creating incentives for providers to be efficient, and it is a mechanism far better suited to VRS and IP Relay than a competitive bidding scheme. While price caps will encourage efficient entry and competition to sign up new users, the use of competitive bidding, as described

increase in the reimbursement rate. As a result, under a cost-of-service approach providers would be far more likely to incur rising per-minute costs in the immediate future than under a price cap approach.

⁹⁹ Parrino Decl. ¶¶ 5-7; Pelcovits Decl. ¶¶ 38-39.

in detail below, will result in limited or no competition; foreclose the possibility of new entry; and ultimately drive up rates.

Finally, all other things being equal, price cap regulation is superior to cost-of-service regulation because it is a market-based and efficient regulatory approach that still allows for adequate oversight while reducing administrative costs.¹⁰⁰ The Commission's historical experience with cost-of-service regulation demonstrates that it requires extremely detailed cost accounting and allocation rules, such as the Uniform System of Accounts in Part 32 of the Commission's rules. Price cap regulation permits the Commission to avoid that regulatory overhang, which benefits no one and imposes costs on providers and regulators, and instead to substitute a far more streamlined method of ensuring that rates are reasonable, which will be less expensive to administer.

C. The Commission Can Readily Implement a Price Cap Regime

As described briefly above, the Commission previously has used a price cap formula consisting of three basic components to regulate the prices charged by AT&T and the largest incumbent LECs: (1) an inflation factor; (2) a productivity measure (sometimes called the "X factor") as well as a consumer productivity dividend; and (3) a provision for cost changes beyond the control of the provider (termed "exogenous" cost changes). The inflation factor is designed to reflect the fact that wages and other expenses will increase due to inflation in the economy as a whole. This adjustment, however, does no more than keep providers whole. The productivity factor establishes an efficiency catalyst for the providers, encouraging increased efficiency over time. The exogenous cost provision is intended to account for the fact that a provider's costs may

¹⁰⁰ See Parrino Decl. ¶ 5; Pelcovits Decl. ¶¶ 20, 65; *see also* Pelcovits Decl. ¶¶ 23, 26 (describing steep administrative costs under a cost-of-service approach).

be increased as a result of a regulatory requirement (*e.g.*, the imposition of the speed-of-answer requirement) or other event beyond the control of the providers and the effects of that cost increase will not be captured by a national measure of inflation. The Commission's price cap plan for incumbent LECs also provided for a performance review after some period of time. The Commission could readily implement a similar approach for VRS and IP Relay.

Price indexing formula. A price cap approach to VRS and IP Relay rate regulation would greatly simplify the annual rate-setting process. Specifically, because the annual adjustment would involve only an adjustment to the indexed rates for VRS and IP Relay, it would eliminate the need for the time-consuming preparation and review of cost and demand forecasts. Instead, the index would be adjusted to account for inflation, productivity gains, and exogenous cost changes, if any.

The GDP Price Index ("GDP-PI"), the same factor used in the telephone company price cap formulas, provides the most reliable measure of inflation for the VRS and IP Relay industries. As explained in the Pelcovits Declaration, GDP-PI is more broadly based than the consumer price index, because it covers the prices of all goods and services in the economy, rather than just the typical basket of goods purchased by consumers.¹⁰¹ Such a broad-based measure of inflation would likely approximate the inflation rate actually experienced by IP Relay providers. The GDP-PI likely would be somewhat lower than the inflation rate experienced by VRS providers, because of the effects of increases in the wages of interpreters.¹⁰²

¹⁰¹ Pelcovits Decl. ¶ 42.

¹⁰² See *id.* ¶ 45 (explaining that labor costs for VRS are likely to increase faster than the costs for the economy as a whole).

Selecting a reasonable productivity factor (or “X” factor in the lexicon of the Commission’s price cap orders) for the VRS and IP Relay industries is a challenging task. In prescribing an X factor for incumbent LECs, the Commission found that the productivity gains of those carriers consistently exceeded the gains achieved by the nation’s economy as a whole. Incumbent LECs, however, enjoy very substantial economies of scale and scope in the provision of local telephone service. They can increase their productivity by increasing the volume of traffic carried over fixed, non-traffic sensitive plant or by expanding the array of products offered over the same plant. The VRS and IP Relay industries, in contrast, are labor-intensive, not capital intensive; the costs of providing VRS and IP Relay depend largely on the hourly wages and other costs of interpreters and communications assistants (“CAs”).

The Commission could undertake a thorough study of the productivity performance of the VRS and IP Relay industries over the past few years, as the Commission did when it formulated its price cap rules for incumbent LECs. Such a study undoubtedly would be costly and time-consuming. Moreover, for the reasons discussed above, it is reasonably likely the results would show that productivity gains in these industries have lagged behind or, at the very least, have not materially exceeded gains in the economy as a whole.¹⁰³

In these circumstances, the Commission could reasonably decide to set an X factor for the VRS and IP Relay services by following an approach it used in setting the annual adjustment to the price cap indices of incumbent LECs. As part of the CALLS plan that the Commission adopted in 2000, the FCC provided that the annual X factor

¹⁰³ See Pelcovits Decl. ¶¶ 44-47.

adjustment to the price indices would be equal to GDP-PI, which has the effect of freezing the cap for the largest LECs.¹⁰⁴ That is, the upward pressure that would otherwise occur because of the inflation factor is offset by the downward pressure from the X factor. Thus, in the case of VRS and IP Relay services, this approach would have the effect of forcing rates for those services downward in real terms over time although they would remain constant in nominal terms.

The Commission previously has included in its price cap formulas an adjustment to provide a consumer productivity dividend.¹⁰⁵ The Commission's theory in the past has been that the introduction of price caps for a minimum period would enhance the incentives of incumbent LECs to exceed their historical productivity gains. The Commission concluded that the cost savings that would result from the enhanced incentives should be shared immediately with rate payers and added 0.5 per cent (0.005) to the X factor to accomplish that result.¹⁰⁶ The FCC's existing approach to VRS and IP Relay rates provides an incentive for providers to become more efficient than the "reasonable" provider. The implementation of a price caps-type approach to VRS and IP Relay rates for a minimum of three years, however, clearly would strengthen those incentives. Consequently, the Commission could reasonably find that in these circumstances, the annual adjustment to account for productivity gains should be increased by 0.5 per cent to reflect the greater efficiency gains it expects providers to achieve over the next three years.

¹⁰⁴ *CALLS Order* ¶ 141.

¹⁰⁵ *LEC Price Cap Report and Order* ¶ 76.

¹⁰⁶ *CALLS Order* ¶ 135.

Thus, under the approach discussed above, the price cap formula for VRS and IP Relay rates would be: $\text{Rate}_{\text{Year } Y} = \text{Rate}_{\text{Year } Y-1} (1 + \text{GDP-PI} - (X + 0.005))$. If $X = \text{GDP-PI}$, then $\text{Rate}_{\text{Year } Y} = \text{Rate}_{\text{Year } Y-1} (1 - 0.005)$. This approach would put pressure on providers to look for efficiency gains, and would discourage inefficient entry during the period the rate is in effect.¹⁰⁷

VRS and IP Relay price caps should also be subject to adjustments for exogenous costs. The Commission should adopt a definition of exogenous costs similar to that used for incumbent LECs. The price cap formula that the Commission applied to incumbent LECs recognized the possibility that carriers may be subject to significant changes in their costs that are neither within the carriers' control nor captured by the nationwide inflation measure, GDP-PI, such as costs caused by new regulatory requirements.¹⁰⁸ Similarly, in any order adopting regulatory changes that affect VRS and IP Relay, the FCC should determine whether the new rules warrant an exogenous adjustment. Any such adjustment should be made at the time the exogenous costs are imposed.

Initial rates. When it established price cap regulation for AT&T and the largest local exchange carriers, the Commission set the initial price indices at the most recently authorized rate levels. If the FCC followed this precedent, it might be reasonable for the

¹⁰⁷ The price cap regime that the FCC adopted for incumbent LECs established indices that governed the prices for an array of services. Since VRS and IP Relay, by contrast, are provided at a single rate, the FCC could elect simply to freeze the compensation rate at its current level for the three year period. At a minimum, this approach would enhance the efficiency incentives of providers to ensure that their productivity gains matched the rate of inflation affecting the industry. As shown in the Pelcovits Declaration, VRS providers in the short term are likely to be subject to upward pressure on key input costs (especially interpreters and outreach), which may well exceed the rate of inflation in the economy as a whole. Pelcovits Decl. ¶¶ 45-47.

¹⁰⁸ See, e.g., *AT&T Price Cap Order* ¶¶ 253-254, 280, 295; 47 C.F.R. §§ 61.45(d)(1)(ii)-(iii).

Commission to use current rates in setting the initial VRS and IP Relay reimbursement rates under a price cap regime. Alternative ways of setting the initial rate might well produce a higher rate.

For the 2005-06 rate year, the Commission concluded that \$6.644 per minute represented a “just and reasonable rate” for compensating VRS providers.¹⁰⁹ The Commission subsequently found that it would serve the public interest to maintain the same VRS rate during the 2006-07 rate year.¹¹⁰ Since \$6.644 has been determined to be a good proxy for the reasonable per-minute costs of a VRS provider during the 2005-07 rate period, it would be a logical choice at which to set the initial VRS rate under price cap regulation.¹¹¹ For example, it is unlikely that providers’ reasonable costs will have fallen significantly by the time any new price cap regime is implemented. As shown in Pelcovits and Johnson declarations, there is upward pressure on key input costs (especially interpreters and outreach) that could easily offset any downward pressure from efficiency gains.¹¹² An alternative would be for the Commission to establish an initial rate based on the projected costs VRS providers submitted for 2006-07 rate year. NECA-provided data indicated that rate would be \$7.01 per minute.¹¹³

¹⁰⁹ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Order, 20 FCC Rcd 12237, ¶ 28 (2005).

¹¹⁰ *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Order, 21 FCC Rcd 7018, ¶ 29 (2006) (“2006 Rate Order”).

¹¹¹ See Pelcovits Decl. ¶ 38.

¹¹² See *id.* ¶¶ 45-47; Johnson Decl. ¶¶ 19-20, 25.

¹¹³ For 2006-07, providers projected total costs of \$508,189,061.88, and total demand of 73,492,796 minutes of use. NECA, “Interstate Telecommunications Relay Services Fund Payment Formula and Fund Size Estimate,” Exh. 1.D (May 1, 2006). Adjusting the

The Commission should set the initial per-minute rate for IP Relay at the current rate of \$1.293.¹¹⁴ The Commission has adopted a separate IP Relay rate only for the 2005-06 and 2006-07 rate years; previously, the IP Relay rate was the same as the TTY rate. Notwithstanding this changed approach, the rate for IP Relay has been relatively stable since the Commission's approval of the service as a form of TRS in April 2002. In fact, during the past four rate years, the IP Relay rate has clustered within a tight range of 12 cents,¹¹⁵ with the current rate of \$1.293 falling at the lower end of that range. This clustering provides reasonable assurance that setting the initial price cap rate for IP Relay at the current rate of \$1.293 per minute would be a sound approach.

Performance review. After an appropriate period of time, no less than three years, the Commission should review the performance of any price cap regime for VRS and IP Relay.¹¹⁶ With LEC price caps, the FCC began such a "performance review" after price caps had been in effect for three years.¹¹⁷ The review took a year and resulted in adjustments to the price cap formula, including a change in the productivity offset. The Commission should plan to conduct a similar review beginning, at the earliest, in 2010, that is, toward the end of a three-year period.

Factors the Commission should consider in its performance review include:

resulting cost-per-minute by the 1.4% allowance for working capital yields a per-minute rate of \$7.01.

¹¹⁴ See Pelcovits Decl. ¶ 38.

¹¹⁵ The rates during the past four years have been as follows: \$1.368 for 2003-04; \$1.398 for 2004-05; \$1.278 for 2005-06; and \$1.293 for 2006-07. Each of these rates is within 5% of the average rate of \$1.334 during that period.

¹¹⁶ Pelcovits Decl. ¶ 49.

¹¹⁷ *LEC Price Cap Order* ¶ 20.

- The extent to which VRS is available to all deaf ASL users, and IP Relay is available to all deaf and hard-of-hearing individuals;
- The number of new VRS and IP Relay users added in the three-year period (a useful proxy for VRS could be the number of new videophones installed);
- The extent to which growth in new users is slowing or accelerating (as indicated by the slope of the curve on adding new users);
- The number of interpreters currently employed by VRS providers and available to be hired by providers;
- The status and impact of ASL interpreter training programs;
- The number of providers that have entered and exited the VRS and IP Relay businesses during the three-year period, and the principal reasons precipitating such entry or exit (to the extent such reasons can be determined); and
- Trends in the service quality of VRS and IP Relay (if the price cap is too tight, one would expect to see degradation in service quality).¹¹⁸

Any adjustments to the price cap formulas for VRS and IP Relay would be prospective only, and would be based on the results of the three-year performance review.¹¹⁹ If the data show that usage for those services has essentially peaked and that both services are fully available, the FCC may choose to shift its focus from growing VRS and IP Relay to maintaining current levels of usage and improving service quality. In such an event, the size of the Fund would level off.

V. BECAUSE THE CURRENT COST-OF-SERVICE APPROACH DOES NOT ALIGN PROVIDERS' INCENTIVES WITH THE PUBLIC INTEREST, THAT APPROACH COULD BE CONTINUED ONLY IF IT WERE SIGNIFICANTLY MODIFIED

A price cap regime is manifestly superior to a cost-of-service approach for VRS and IP Relay. If the Commission were nonetheless to elect to continue the latter

¹¹⁸ See Pelcovits Decl. ¶ 50.

¹¹⁹ See *id.* ¶ 51.

approach, it would have to adopt and implement significant modifications and recognize that the likely result would be higher rates and a much greater regulatory burden on providers, NECA, and the FCC.

As explained below, the current cost-of-service approach to regulating VRS and IP Relay rates suffers from a number of problems, each of which compounds the effects of the others.¹²⁰ Certain of these problems are endemic to cost-of-service regulation and therefore could not be rectified even if the Commission were to modify the existing scheme. Other problems could be ameliorated with some effort, but only at the expense of increasing significantly the administrative burden on the FCC and providers, and the VRS and IP Relay rates.

A. The Current Methodology Suffers from Certain Inherent Flaws

As explained in the attached Pelcovits and Parrino declarations, the current methodology suffers from several problems that are inherent in cost-of-service regulation. For example, because the current methodology ties rates to costs, it blunts providers' incentives to pursue cost-saving efficiencies.¹²¹ This failure to achieve

¹²⁰ To be sure, under the current system, the Commission has managed to make some progress in advancing the goals of full availability and maximum efficiency. For example, the FCC's rate decisions for VRS over the past two years have encouraged the continued expansion in the availability of VRS to the deaf community; created an incentive for providers to continue to improve the efficiency of their offerings so that their performance exceeds the efficiency of a "reasonable" VRS provider; and attracted new entry that will intensify competition among providers. Those effects, in turn, have benefited rates in two ways: the VRS rate has been reasonably fair during the 2005-07 rate period; and it has not varied arbitrarily during that period.

¹²¹ Pelcovits Decl. ¶ 24. The Commission has done its best to mitigate this problem under the current methodology. Specifically, the Commission chose to set VRS and IP Relay rates based on the costs incurred by a hypothetical reasonably efficient provider. Providers therefore have some incentive to lower their costs – *i.e.*, to the extent they can bring their costs below that of the hypothetical provider, providers can retain the benefit of their efficiency gains. This incentive, however, is diminished by the knowledge that

available efficiencies is termed “X-Inefficiency” and has been documented in a large body of economic literature.¹²² Traditional cost-of-service regulation also distorts the investment incentives of firms, influencing the choice between different inputs. For example, it may cause labor-intensive businesses, such as VRS and IP Relay providers, to over-invest in relatively minor capital-intensive aspects of their business while under-investing in critical labor-intensive areas.¹²³

Cost-of-service regulation also inherently imposes large administrative burdens and costs on regulators and providers alike.¹²⁴ Because a cost-of-service regime requires regulators to exercise their own judgment about the propriety of different expenditures of regulated firms, regulators must require companies to keep uniform systems of account, according to stipulated procedures and rules, and subject to audit.¹²⁵ The process of establishing a uniform system of accounts is costly, as is the process of reviewing and passing judgment on the costs incurred by the regulated firm.¹²⁶ In practice, moreover, regulatory agencies have not been very successful at evaluating the reasonableness of firms’ costs.¹²⁷ The inherent complexity of the data submitted under such a process, combined with the difficulty of divining what constitutes a “reasonable” or permissible

aggressive cost saving efforts may lower the rate attributed to the hypothetical reasonably efficient provider in the forthcoming rate year.

¹²² *Id.* (citing sources).

¹²³ *Id.* ¶ 25.

¹²⁴ *Id.* ¶ 26; Parrino Decl. ¶ 6.

¹²⁵ Pelcovits Decl. ¶ 26.

¹²⁶ *Id.*

¹²⁷ *Id.*

cost, fosters a litigious response to the decisions reached by regulators, thereby imposing more administrative costs and burdens on all parties.

The inherent flaws of cost-of-service regulation are readily apparent in the methodology currently used by the FCC to set VRS and IP Relay rates. Providers do not have adequate incentives to operate efficiently or to invest in critical labor-intensive projects, such as the recruitment and training of VRS interpreters and the extension of VRS and IP Relay to new users.¹²⁸ In addition, because VRS and IP Relay providers pursue a wide range of business models (some are traditional telecommunications carriers, some provide only TRS service, and some are Internet-based providers), it is extremely difficult to establish a *uniform* system of accounts that applies to all such providers.¹²⁹ The current methodology also imposes substantial administrative burdens. For example, providers must prepare and file complex financial documents reflecting both their historical and projected costs, and NECA and the FCC then must carefully review, and in some cases audit, those filings. The inherent difficulty of determining the reasonableness of providers' costs has also caused NECA and the FCC frequently to modify the rate setting process and the determination of what costs are allowed to be included in the calculation of rates. The resulting uncertainty has made it difficult for providers to implement long-range business plans, make long-term investments, or expand the availability of their service.¹³⁰

¹²⁸ Parrino Decl. ¶ 6; Pelcovits Decl. ¶¶ 24-25.

¹²⁹ Parrino Decl. ¶ 7.

¹³⁰ *Id.* ¶ 8.

B. Retaining a Cost-of-Service Approach Would Require Significant Changes

In addition to these inherent problems, the existing rate methodology suffers from several flaws that the Commission could, with some effort, address. For example, under any cost-of-service system, it is critical that the costs incurred by providers be reported in a manner that is consistent from provider to provider, and at an appropriate level of detail, so as to allow meaningful analysis by NECA and the Commission.¹³¹ The current system thwarts this goal in two ways: by requiring providers to assign their reported costs to “accounts” that are not aligned with the costs actually incurred in the provision of VRS and IP Relay; and by failing to provide clarity regarding what costs the FCC will include in determining the applicable reimbursement rate and what costs should be included in each account.¹³² The Commission would need to develop a new set of accounts and provide clearer guidance regarding the costs that should be included in each account.¹³³

If the Commission were to retain a cost-of-service approach, it would also be essential to provide greater rate stability by adopting a three-year rate period, instead of the one-year period currently in place. Doing so would encourage providers to operate more efficiently, facilitate entry by new providers, foster long-range planning and investment, and reduce the administrative burden borne by providers, NECA, and the FCC.¹³⁴

¹³¹ *Id.* ¶ 11.

¹³² *See id.*

¹³³ *Id.* ¶¶ 11-13.

¹³⁴ *Id.* ¶ 32. In other contexts, the FCC has found that extending the time frame on a requirement, or choosing a longer rather than shorter time frame, is appropriate where doing so would enhance incentives for companies to operate more efficiently or

Although such efforts would certainly improve the current cost-of-service system, the Commission would have to take at least two other steps to make that system arguably consistent with the mandates of section 225: (i) allow providers to recover certain key costs that are currently disallowed; and (ii) reject proposals to disallow or limit certain costs that are currently allowed.¹³⁵

To reform the current methodology, the Commission would have to allow providers to recover certain types of cost that are necessary to achieving the key goals of section 225.¹³⁶ For example, the current methodology does not treat the costs of installing end-user equipment and training individuals to use that equipment as reimbursable expenses or capital expenditures. This position is not consistent with the

implement business plans, or would reduce administrative burdens. *See, e.g., Regulatory Reform for Local Exchange Carriers Subject to Rate of Return Regulation*, Report and Order, 8 FCC Rcd 4545, ¶ 21 (1993) (moving from an annual tariff filing requirement to a biennial filing requirement will enhance carriers' incentive to manage costs and stimulate demand to maintain or improve earnings); *Review of Part 87 of the Commission's Rules Concerning the Aviation Radio Service*, Report and Order and Further Notice of Proposed Rulemaking, 18 FCC Rcd 21432, ¶ 40 (2003) (extending license period from five to ten years for non-aircraft stations will provide incentives for investment in licensed facilities and reduce administrative burdens borne by licensees and the FCC); *Amendment of the Commission's Space Station Licensing Rules and Policies*, Notice of Proposed Rulemaking and First Report and Order, 17 FCC Rcd 3847, ¶¶ 141, 143 (2002) (extending license term from ten to fifteen years will reduce administrative burdens); *see also Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696, ¶ 151 (1999) (reexamining the national list of network elements that are subject to the unbundling obligations of the Act every three years, instead of on a rolling, *ad hoc* basis, will provide competitors with "reasonable certainty for a period of time that is sufficient time to implement their [business] plans").

¹³⁵ Even if the FCC were to take these steps, it could not eliminate the two problems of weak market incentives and high administrative costs. As described above, those problems are inherent features of cost-of-service regulation. It is not clear whether any rate methodology beset by such problems can fully satisfy the requirements of section 225.

¹³⁶ Parrino Decl. ¶ 14.

statutory goals of full availability and functional equivalency.¹³⁷ The current methodology also does not fully reimburse research and development expenses incurred by providers, even though research and development is critical to advancing the statutory goals of functional equivalence, maximum efficiency, and improved technology, and to implementing a viable E911 solution for VRS and IP Relay users.¹³⁸ Nor does the current methodology fully reimburse expenses associated with expanding the pool of available VRS interpreters. Achieving this result would allow providers to meet demand from new users (as required by the universal service mandate of section 225), and to do so in a cost-effective manner (as required by the efficiency mandate of section 225).¹³⁹

Finally, and perhaps most egregiously, the current methodology fails to reimburse providers for a normal profit, and instead allows providers to recover only a return on capital. The FCC has decided that the best way to advance the goals of section 225 is to have VRS and IP Relay providers compete for users and minutes. In order for this competitive model to give providers the proper incentives, however, the rates for VRS and IP Relay must be set at the costs incurred by a hypothetical reasonably efficient provider of those services. The FCC has generally viewed economic costs as including a reasonable profit.¹⁴⁰ Here, such profits are necessary to compensate for the risks borne

¹³⁷ *Id.* ¶¶ 16-18.

¹³⁸ *Id.* ¶ 15.

¹³⁹ *Id.* ¶¶ 19-25.

¹⁴⁰ See, e.g., *Further Report On the Packaging and Sale of Video Programming Services To the Public*, Report, Economic Appendix at 59, ¶ 26 n.15 (Feb. 9, 2006), available at: <http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-263740A1.pdf> (“‘Cost’ is generally assumed to include a reasonable profit, so that content providers have an incentive to produce programming.”); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 Rate Regulation*, 9 FCC Rcd 1164, ¶ 49 n.80 (1993) (“A competitive rate is generally one that reflects actual cost

by VRS and IP Relay providers in a rapidly evolving competitive environment.¹⁴¹ From an economic perspective, therefore, the costs of a hypothetical reasonably efficient provider must include reasonable profits. Excluding such profits from rates would deter new entry and undercompensate existing providers, failing to give them the ability and incentive to behave as firms would under normal, competitive conditions where reasonable profits can be earned.¹⁴² These ill effects would be particularly pronounced in the VRS and IP Relay industries, both of which are labor-intensive, rather than capital-intensive. In such businesses, simply allowing for a return on capital, without any other kind of profit margin, denies providers the ability to make a reasonable profit and, in the long run, causes firms to exit the business.¹⁴³ Any reformed cost-of-service approach therefore must include a reasonable profit margin.

As part of any effort to rehabilitate the current system, the Commission also would have to reject proposals to disallow or limit other costs, such as costs associated with advertising, marketing, and outreach.¹⁴⁴ As explained in the Parrino declaration, expenses for branded advertising and marketing are incurred in the normal course of any competitive business, and are particularly critical to the business models of VRS and IP

including a reasonable profit.”); *id.* ¶ 42 (“Under the ‘actual cost’ standard, cable operators recover their costs including a reasonable profit. This will result in rates comparable to those that would exist in a competitive environment . . .”).

¹⁴¹ Pelcovits Decl. ¶ 56.

¹⁴² See Parrino Decl. ¶ 26. The FCC does not even reimburse providers for all costs other than a normal profit. For example, the costs of distributing free videophones and training users how to use that equipment is not reflected in the VRS rate.

¹⁴³ Pelcovits Decl. ¶¶ 52-56; Parrino Decl. ¶¶ 26, 28.

¹⁴⁴ See *Further Notice* ¶¶ 33-37.

Relay providers.¹⁴⁵ For example, without advertising and marketing, very few deaf and hard-of-hearing persons or interpreters would hear of outreach events. In addition, advertising and marketing is highly useful to recruiting new interpreters and CAs, and is a logical expenditure under the new interoperability regime, in which VRS providers are encouraged to urge ASL users to use their service instead of that of other providers.¹⁴⁶ Accordingly, advertising and marketing expenses should be reimbursed from the Fund under any cost-of-service approach.¹⁴⁷ Outreach also is necessary to achieve the statutory goal of 100 percent access to VRS and IP Relay, to expand the pool of available interpreters and CAs, and to educate the hearing community about those Relay services.¹⁴⁸ Since VRS and IP Relay are relatively new and rapidly growing forms of TRS that have low penetration rates, it does not make sense to base reimbursement for outreach on a percentage of providers' total costs, as suggested in the *Further Notice*.¹⁴⁹ Failure to allow full recovery of all such costs would perpetuate the current scheme's

¹⁴⁵ Parrino Decl. ¶¶ 33-36. Other FCC universal service programs permit providers to recover certain branded marketing expenses. For example, the calculation of High Cost Federal Universal Service support for carriers eligible to receive Local Switching Support includes an account for carrier-specific "product advertising," which is defined as "costs incurred in developing and implementing promotional strategies to stimulate the purchase of products and services." See *USAC High Cost Forms, Local Switching Support Instructions for 2006 Support Calculation*, available at: http://www.universalservice.org/_res/documents/hc/pdf/LSS_Instructions.pdf (Account 6610 – Customer Services Marketing Expense); 47 C.F.R. §§ 54.301(b), 32.6610 (defining "customer services marketing expenses" as including "product management and sales" and "product advertising"), 32.6613 (defining "product advertising").

¹⁴⁶ Parrino Decl. ¶ 34-35.

¹⁴⁷ *Id.* ¶ 36.

¹⁴⁸ *Id.* ¶¶ 37-39.

¹⁴⁹ *Further Notice* ¶ 37.

failure to encourage providers to operate efficiently and expand the availability of VRS and IP Relay, as required by section 225.

VI. USE OF TRUE-UPS, HISTORIC COSTS, OR COMPETITIVE BIDDING WOULD BE COUNTERPRODUCTIVE

A. The FCC Should Not Use a “True-Up” Scheme to Adjust Reimbursement for VRS and IP Relay

A “true-up” scheme would create the wrong incentives for providers, make it harder for providers to attract capital, place a heavy administrative burden on regulators and providers, and put upward pressure on the rate and the Fund.¹⁵⁰ In light of these drawbacks, the Commission should not subject VRS and IP Relay to a true-up process.

As an initial matter, the FCC’s interest in a true-up scheme for VRS appears to arise from its belief that providers’ demand forecasts for that service have generally been lower than actual demand.¹⁵¹ In early years, demand for any service is likely to be unpredictable. As providers gain experience, demand is likely to be more predictable. Sorenson, for example, has become increasingly adept at projecting demand, both for its own service and for the VRS industry as a whole. The increased accuracy of demand forecasts allays the main concern that appears to underlie the FCC’s interest in a true-up for VRS.

¹⁵⁰ Parrino Decl. ¶¶ 43-45; Pelcovits Decl. ¶ 35.

¹⁵¹ See *Further Notice* ¶ 29. The FCC also sought comment on whether providing compensation greater than providers’ actual costs “can be reconciled” with section 225. *Id.* Although section 225 provides guidance regarding the recovery of the “costs caused by” inter- and intrastate TRS, Congress was silent regarding the reimbursement of providers. See 47 U.S.C. § 225(d)(3); see also *Further Notice* ¶ 4. Therefore, the Commission is free to adopt any reasonable methodology governing the reimbursement of TRS providers, so long as that methodology advances the stated goals of section 225.

A true-up system would undermine any incentive for VRS and IP Relay providers to improve their efficiency or innovate.¹⁵² At least under traditional cost-of-service regulation, providers may have some incentives – albeit very modest ones – to improve efficiency during the rate year since they would be allowed to retain any gains realized during that rate year, even though the rates for the next year would have to be adjusted downward to reflect those gains. A true-up scheme, however, would discourage even modest efforts to improve efficiency, since providers would be required to remit any savings back to the Fund.¹⁵³ To avoid such remittances, providers would be inclined to pay interpreters more or become less efficient.¹⁵⁴ The prospect of having to return savings would also increase investors’ perceived risk of the VRS or IP Relay businesses, making it harder for providers to attract capital.

Further, a true-up scheme would add significantly to, rather than reduce, the existing burdens of administering the Fund.¹⁵⁵ Under a properly administered true-up scheme, regulators must carefully review and perhaps audit the yearly costs reported by each provider to determine whether the provider operated efficiently, whether the provider’s costs are reasonable, and whether a true-up is necessary. Providers and the FCC would have to continue to incur the costs of preparing, filing and reviewing demand and cost estimates for the upcoming rate year. In addition, providers would have to incur the costs of preparing and filing post-year reports detailing their actual costs and demand,

¹⁵² Parrino Decl. ¶ 44.

¹⁵³ See Pelcovits Decl. ¶ 35 (by removing any incentive for providers to cut costs, a true-up scheme would create “the ‘nightmare’ scenario’ of an absolutist cost-of-service regulation, where providers were not even allowed to retain any cost savings from the year in which they were created”).

¹⁵⁴ Parrino Decl. ¶ 44; *see also* Pelcovits ¶ 35.

¹⁵⁵ *Id.* ¶ 45.

and those reports then would have to be reviewed (and perhaps audited) by the FCC. A true-up scheme would also require more detailed accounting rules, further increasing the administrative burdens borne by providers and the Commission alike.

Finally, if a true-up regime were adopted, it would have to work symmetrically, such that providers would refund any “overpayments” from the Fund and would also recover additional funding for their underestimated costs.¹⁵⁶ Under a symmetrical system, providers would have no incentive to maintain costs below the reimbursement rate – indeed, their incentive would be to err on the side of spending in excess of the compensation rate since they would also be compensated for those costs.¹⁵⁷ Likewise, a symmetrical system would give providers no incentive to reduce costs. A true-up system would therefore put upward pressure on the rate and on the Fund.¹⁵⁸

¹⁵⁶ Under a non-symmetrical true-up system, providers would have powerful incentives to overestimate costs and to shift costs from future years to the current year, by, for example, prepaying expenses. Given these incentives, the Commission would have to expend significant administrative resources in an effort to police providers under a non-symmetrical system. Although a symmetrical true-up would be fairer to providers and less burdensome to police, it also would have the drawback that firms would have no incentive to control costs.

¹⁵⁷ If the Fund did not provide additional funding to firms that underestimate costs, providers would have a very powerful incentive to overestimate their costs and underestimate demand to protect themselves from the risk of not meeting their targeted costs and demand.

¹⁵⁸ A true-up also would hamper efficient administration of the Fund. For example, if the actual costs incurred by all providers in a particular rate year exceeded forecasted amounts, the FCC would have to recover both the added costs from the prior rate year as well as the costs of the current rate year from the current year’s fund. The work needed to make such adjustments could add significant costs to the administration of the Fund.

B. The FCC Should Not Use Historic Costs to Set VRS and IP Relay Rates

The Commission also should not base VRS and IP Relay rates on “actual reasonable historical costs” but should continue to use costs projected by providers.¹⁵⁹ A methodology based on actual historical costs has a high likelihood of resulting in unfair treatment of providers, would discourage providers from operating efficiently, and would not reduce administrative burdens.¹⁶⁰

If providers were to incur rising per-minute costs for the immediate future, basing rates for a particular year on the prior year(s) actual costs would result in providers receiving compensation that is not sufficient to cover their expenses during that year.¹⁶¹ Absent a true-up, such undercompensation is likely to force many providers to exit the business and deter new providers from entering the business in the first place.¹⁶² In the VRS business, such results would undermine, and perhaps destroy, the competitive paradigm that has hitherto helped advance the statutory goals of full availability, functional equivalency, maximum efficiency, and technological advancement.

In addition, basing rates on historic costs would increase incentives for providers to raise costs, thereby putting upward pressure on VRS and IP Relay rates, without reducing the administrative burdens of the rate setting process. For example, if a provider knows that the rate at which VRS will be compensated during future rate periods

¹⁵⁹ *Further Notice* ¶¶ 22, 29.

¹⁶⁰ *See* Parrino Decl. ¶¶ 40-42. As Commissioner Parrino also attests, her 22-year tenure at the Public Service commission of Wisconsin (including seven years as Chairman) has led her to “consistently support[] and advocate[] the use of projected costs for establishing rates” instead of historic costs). *Id.* ¶ 40.

¹⁶¹ *Id.* ¶ 40.

¹⁶² As explained above, however, a true-up scheme would be inadvisable because it would harm the public interest in various ways.

will be based on the costs it incurs during the present rate period, that provider will have a strong incentive to increase its present costs as much as possible. To deter such actions, regulators would be forced to wage a costly – and probably futile – rear-guard campaign in an effort to assess the accuracy and reasonableness of each cost incurred by each provider and determine whether each provider operated efficiently, and to adjust future rates accordingly.

C. The FCC Should Not Use Competitive Bidding to Set the VRS Rate

The *Further Notice* seeks comment on using a bidding process to set the VRS rate, and allowing one or more firms to provide service based on the lowest bid rate.¹⁶³ As explained below, a bidding process would create the wrong incentives for providers, and over time would cause the VRS rate to increase and quality of service to decrease.

In implementing competitive bidding in other contexts, the Commission has found it necessary to adopt complex rules and procedures that are carefully tailored to each specific context.¹⁶⁴ In the *Further Notice*, however, the Commission devotes only a single, elliptical sentence to describing possible bidding mechanisms. As a conceptual matter, however, competitive bidding is an extremely poor as well as risky approach to the establishment of federal reimbursement rates for TRS. If the FCC seeks to harness market incentives, it would be far preferable to use the price cap approach described above.

¹⁶³ *Further Notice* ¶ 28.

¹⁶⁴ The general (non-service specific) procedures for competitive bidding are codified in fourteen separate FCC rules, covering a range of complex topics, including: eligibility; bidding design options; bidding mechanisms (*e.g.*, sequencing, grouping, reserve price, bid increments); anti-collusion; upfront payments; default; petitions to deny; disclosure and reporting requirements; and designated entities. *See* 47 C.F.R. §§ 1.2101-1.2114. This does not even include the service-specific rules, codified elsewhere.

For example, in order for a process to promote *competitive* bidding, the bidders must have an incentive to compete with each other by bidding down the rate. This incentive, in turn, depends on each bidder having confidence that the winning bidder(s) will be awarded something of value, such as the exclusive right to serve a certain geographic area or a certain group of users. It is quite possible that providers would place no value on winning the right to be one of *several* firms providing national VRS at the lowest bid.¹⁶⁵ The *Further Notice* compounds this problem by failing to address whether the winning bidder(s) would be awarded some other valuable right, such as a guaranteed share of VRS minutes. Absent the assurance of some valuable right to be awarded to the lowest bidder(s), there would be no incentive for any bidder to bid down the VRS rate during an auction.¹⁶⁶

If the FCC were to attempt to avoid this problem by adopting a bidding mechanism that guarantees all (or some of) the market to the winner(s), it would simply be replacing a bad result with a worse one. For an IP-based service with national coverage, it would be difficult, if not impossible, to guarantee a predetermined share of the market to firms based on their bids. Moreover, if the winning bidder(s) were to be awarded such a guarantee, VRS users would lose all or much the opportunity to choose between providers. As a result, the winning bidder(s) would be unlikely to have an

¹⁶⁵ Pelcovits Decl. ¶ 62.

¹⁶⁶ *Id.* (explaining that the result would likely be a higher rate than today's compensation rate). For example, under a process in which all firms are allowed to participate in the market at the "winning price," the bidding is unlikely to lead to a low price. Even a low-cost firm will not find it to be a good strategy to bid down the price in order to drive other firms out of the market. Under most circumstances, the low-cost firm will earn greater profits by bidding high and then competing for customers on the basis of quality, or by increased marketing of its service. Moreover, if the other firms now participating in the market are unable to expand capacity and readily serve the low-cost firm's customers, then the low-cost firm has even less to gain by submitting a low bid.

incentive to provide adequate service to all who need or want it. The easiest way for a firm to lower its costs and justify a lower bid would be to provide a lower-quality service; with a guaranteed market share, the winner(s) of the bid would have no (or a limited) incentive to provide acceptable service to all who want or need it. This erosion of the incentive to provide adequate service would likely be coupled with the equally bad result of higher rates. As explained below, after the first auction, the losing bidders would almost certainly exit the VRS business.¹⁶⁷ With fewer participants in future auctions, the surviving company or companies would have the opportunity and incentive to raise their bid prices in subsequent auctions.¹⁶⁸

Competitive bidding, in short, is not a useful technique in a growing market where new entry is desired, and competition should be harnessed to produce efficiency gains. Rather, the FCC should use the price cap approach described above to achieve increased efficiency, while continuing consumer choice and competition. Rates will almost certainly be higher under a competitive bidding regime than they would be under the price cap approach described above. If the Commission failed to award something of value to the winning bidder(s), the VRS rate yielded by the competitive bidding process would be too high. If the Commission did award something of value, however, the quality of service provided by the winning bidder(s) would be too low, and the VRS rate would sharply increase in subsequent auctions. The cursory treatment of competitive

¹⁶⁷ *Id.* ¶ 63. Even the prospect of an auction that would result in one or a few winners would have harmful effects. For example, prior to such an auction, many providers would likely have greater difficulty attracting investment from capital markets, or would have to pay higher interest on any investment. The resulting squeeze on capital could cause providers to exit the business even before an auction were completed.

¹⁶⁸ *Id.*

bidding in the *Further Notice* gives no indication that the Commission could avoid either horn of this dilemma under a bidding scenario.

There are additional conceptual problems with competitive bidding. Presumably, the Commission would want any bidding process to be open only to those participants who could provide VRS in conformity with the applicable mandatory minimum standards. The *Further Notice* does not address, however, whether providers would have to meet any minimum qualifications in order to bid, or identify what those qualifications might be. The Commission's silence on this issue gives rise to a number of questions. For example, could a provider with very few interpreters bid to serve a major part of the traffic? How would the Commission ensure that the winning bidder was actually capable of providing the quality of service required under the FCC's rules?

The *Further Notice* also fails to address how a bidding process would ensure that a sufficient number of VRS providers remain financially viable to allow market forces to continue to operate. In most bidding situations (*e.g.*, government contracts, requests for proposals ("RFPs") for telecommunications services), the participants do not risk their entire business on one bid. Rather, even if they fail to submit a winning bid, they are likely to remain in the market serving other customers and are therefore able and willing to participate on a regular basis in new auctions. In those situations, the periodic opportunity to bid gives firms the incentive to operate efficiently in order to be able to outbid rivals. In addition, if the same firms participate in the bidding year after year, they have an incentive to provide high quality service in order to maintain a good reputation.

In stark contrast to the typical bidding scenario, the mechanisms sketched in the *Further Notice* would provide little if any opportunity for multiple VRS providers to

remain financially viable, and, at a minimum, would cause many providers that currently offer the service to go out of business. Today, nine providers of VRS receive compensation from the Fund¹⁶⁹ and more are certified to provide VRS.¹⁷⁰ Under the bidding proposals described in the *Further Notice*, however, only a few providers capable of providing service at the lowest bid rate would be permitted to provide VRS.¹⁷¹ At most, only a few providers are likely to be able to recoup their costs of providing VRS at the lowest bid rate. The remaining providers either would have to mothball their operations until the next national auction (something that would not be financially feasible for most firms) or simply exit the VRS business on a permanent basis.

Without more explanation, therefore, it appears that adoption of the competitive bidding scenarios proposed in the *Further Notice* would reduce the number of VRS providers and thereby attenuate – if not eliminate – the market forces that currently encourage providers to compete for users. Any such result would have disastrous consequences. The competitive paradigm under which VRS has been provided since its designation as a compensable Relay service has allowed it to flourish, and has provided incentives for providers to fulfill the statutory mandates of section 225. This paradigm has worked so well because the Commission has set a reasonable per-minute price at which VRS will be compensated, and has left users free to choose their preferred

¹⁶⁹ See NECA, “TRS Fund Performance Status Report” (Oct. 19, 2006), *available at*: <<http://www.neca.org/media/0906AugustdataTRSSstatus.pdf>>. Those providers are identified as AT&T, Communications Access Center, Hamilton Relay, Inc., Hands On Video Relay Service, Inc., Healinc Telecom (which only recently began receiving compensation), MCI, Nordia, Sorenson, and Sprint Corporation, Inc.

¹⁷⁰ Companies that recently have been certified for compensation from the Interstate TRS Fund include GoAmerica, Inc. and Snap Telecommunications, Inc.

¹⁷¹ *Further Notice* ¶ 28.

provider(s) from among the growing number of firms that offer the service. Under the auction schemes sketched in the *Further Notice*, however, the Commission would abandon this competitive paradigm: the FCC no longer would set a reasonable VRS rate that would enable multiple providers to compete for users based on factors such as quality of service and technology, but instead would effectively coronate a small number of government-anointed oligopolists that would no longer be subject to the discipline of market forces. Knowing that losing bidders would soon exit the business, the winning bidder(s) would have an incentive to provide service for the shortest possible term and then bid up the price (unconstrained by competing bids from the exited firms) during the next auction, once the initial contract has expired.¹⁷² The surviving provider(s) would have little, if any, incentive to invest in new technology or in solutions that would increase the pool of available interpreters or expand the availability of VRS to more end users. The prospect of more expensive, lower quality, and less available VRS, combined with the need for more complex and intrusive regulation by the FCC, should cause the Commission to reject proposals to adopt an auction scheme for VRS.

VII. THE MARS PLAN SHOULD NOT BE APPLIED TO EITHER IP RELAY OR VRS

If the Commission were to decide to adopt the Multi-state Average Rate Structure (“MARS plan”) proposed by Hamilton, or some variant of that plan, it should not apply that new methodology to either IP Relay or VRS. Under Hamilton’s proposal, the MARS plan would be limited to developing the compensation rate for interstate TTY.¹⁷³ And, as the FCC recognizes, the MARS plan “could not apply” to VRS and IP Relay “because

¹⁷² Pelcovits Decl. ¶ 63 (explaining that any firm attempting to enter or reenter the industry would incur higher costs than the incumbent).

¹⁷³ *Further Notice* ¶ 17.

there is not state data upon which to base a rate calculation.”¹⁷⁴ Lacking any such data, the Commission would have no rational basis for applying the MARS plan to either service.

Nor should the FCC attempt to apply the MARS plan to IP Relay indirectly by setting the compensation rate for IP Relay at the same level as the rate for traditional TRS.¹⁷⁵ As observed in the *Further Notice*, there appears to be a cost disparity between the two services.¹⁷⁶ Given this disparity, the Commission should not rely on the intrastate TTY rate to set the interstate IP Relay rate.

It is even clearer that the MARS plan is completely inappropriate for VRS. Not only is there no intrastate data on VRS, but the VRS cost structure is unique and the costs of providing VRS bear little resemblance to the costs of providing TTY or other forms of TRS.¹⁷⁷ Thus, the intrastate rates of other forms of TRS have little if any bearing on the interstate VRS rate.

VIII. THE FCC SHOULD ADOPT MEASURES TO COMBAT WASTE, FRAUD, AND ABUSE

In the *Further Notice*, the Commission invites comment “on any other ways to achieve more fair and efficient administration and management [of the Fund], as well as

¹⁷⁴ *Id.* ¶ 17 n.60.

¹⁷⁵ *See id.* ¶ 19.

¹⁷⁶ *Id.*

¹⁷⁷ *See, e.g., Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, Report and Order, Order on Reconsideration, and Further Notice of Proposed Rulemaking, 19 FCC Rcd 12475, ¶ 20 (describing the Commission’s conclusion that given “the unique characteristics of VRS, a separate reimbursement rate for VRS should be calculated”) (citing *Telecommunications Services for Individuals with Hearing and Speech Disabilities – Recommended TRS Cost Recovery Guidelines/Request by Hamilton Telephone Company for Clarification and Temporary Waivers*, Memorandum Opinion and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 22948, ¶ 22 (2001)).

to deter and detect waste, fraud, and abuse.”¹⁷⁸ Although good controls are currently in place, the FCC should add more to ensure the integrity of TRS and the Fund.

VRS providers already supply a substantial amount of cost and demand information as well as compliance and monthly minutes-of-use data to NECA. Both NECA and the Commission possess authority to audit VRS providers should concerns or irregularities arise.¹⁷⁹

The Commission should supplement these existing protections with additional measures. Specifically, the FCC should require automated electronic counting of minutes. The Commission’s rules provide that only conversation minutes (not call set-up, ringing, waiting for an answer, wrap-up, unanswered or busy calls) are compensable.¹⁸⁰ Neither the Commission’s rules nor NECA’s procedures specify the technology that must be utilized to count the conversation minutes of VRS calls, however. Automated counting of VRS conversation minutes by VRS providers would promote a more transparent and accurate means of identifying compensable services, would reduce the potential for human error, and would facilitate any audits by the Commission or NECA. Automated counting would also provide a safeguard against fraud and tampering: For example, if counting were automated, VRS interpreters would not be able to retroactively change conversation minutes.

As Commissioner McDowell suggested, the Commission also should require providers to adopt safeguards that will lessen the extent to which any cost recovery

¹⁷⁸ *Further Notice* ¶ 49.

¹⁷⁹ 47 C.F.R. § 64.604(c)(5)(iii)(E).

¹⁸⁰ *Id.*; see also 47 C.F.R. § 64.604(c)(5)(iii)(C).

methodology is susceptible to fraud.¹⁸¹ This is a particular concern for IP Relay. As Sorenson and others have explained in a pending rulemaking proceeding (the “*IP Fraud Proceeding*”),¹⁸² the usefulness of IP Relay has increasingly been threatened by the fraudulent use of the service, typically by a person located outside the United States who places an IP Relay call to a U.S. merchant, and then uses a stolen or fake credit card to order merchandise to be shipped outside the United States.¹⁸³ Unless the Commission acts to address this problem, merchants will become less willing to accept IP Relay calls, and, as a result, deaf and hard-of-hearing Americans will no longer be able to rely on IP Relay as a means of conducting important transactions in their day-to-day lives. Under the ADA, the Commission is required to ensure that this outcome does not in fact occur.

The record in the *IP Fraud Proceeding* reflects a number of anti-fraud measures that providers may take, including:

- Blocking all international calls;
- Developing criteria for identifying fraudulent calls, and notifying the called party (e.g., a merchant) during the call and asking if the call should be terminated;
- Recording the IP address or other identifying information of a caller who has placed fraudulent calls in the past and using such information to identify or monitor future calls;
- Undertaking a systematic program for educating merchants about the fraud problem, and developing some “best practices” they can adopt (e.g., asking for a four-digit security number on credit cards); and

¹⁸¹ See *Further Notice* at 36, Statement of Commissioner Robert M. McDowell (FCC should ensure that any rate methodology does not “fall prey to waste, fraud, and abuse”).

¹⁸² *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities, Misuse of Internet Protocol (IP) Relay Service and Video Relay Service*, CG Docket No. 03-123, Further Notice of Proposed Rulemaking, 21 FCC Rcd 5478 (2006).

¹⁸³ See, e.g., Comments of Sorenson Communications, Inc. at 1-2 (July 3, 2006) (“Sorenson IP Fraud Comments”).

- Allowing CAs to terminate harassing calls from hearing or non-hearing individuals.¹⁸⁴

The Commission should promptly clarify that providers are authorized to implement the foregoing safeguards, and should implement them, in order to prevent and deter IP Relay fraud.

IX. THE FCC SHOULD MAKE PROVIDER DATA PUBLICLY AVAILABLE, BUT ONLY IN A SUFFICIENTLY AGGREGATED FORM

In the *Further Notice*, the Commission explains that historically it “has honored requests by providers submitting projected cost and demand data to treat that information as confidential” by addressing such data only in the aggregate or in ways that do not identify individual data of a particular provider.¹⁸⁵ The *Further Notice* seeks comment on “whether the providers’ projected (and/or actual) cost and demand data, or particular categories of the cost and demand data, should be made public.”¹⁸⁶

Sorenson understands the Commission’s and NECA’s need for particularized cost and demand information. It also understands that there are benefits to be gained by receiving informed comments from the public and providers alike as to the reasonableness of proposed VRS rates. However, Sorenson does not believe that the current confidential treatment impairs effective comment on the reasonableness of rates.

¹⁸⁴ See, e.g., Sorenson IP Fraud Comments at 5-14; Comments of AT&T Inc. at 3-4 (July 3, 2006); Comments of Telecommunications for the Deaf and Hard of Hearing, Inc., *et al.*, at 8-9 & n.5 (July 3, 2006); *Ex Parte* Comments of Nordia, Inc. at 1-5 (Sept. 7, 2006); Comments of Sprint Nextel Corporation at 3-7 (July 3, 2006); Comments of Verizon at 7-9 (July 3, 2006); see also Comments of Communication Service for the Deaf, Inc. at 2, 5 & n.5, 8-9 (July 3, 2006) (proposing safeguards for VRS).

¹⁸⁵ *Further Notice* ¶ 43.

¹⁸⁶ *Id.* ¶ 44.

VRS rates are established on an aggregated basis. Often, the debate about the reasonableness of those rates addresses the appropriate *categories* of inputs to or exclusions from the calculations rather than the appropriateness of a particular provider's data. Hence, more individualized data would not promote more meaningful comment on the reasonableness of VRS rates. To be sure, the individual submissions collectively determine the aggregated rate and a particular provider's data can thereby affect the reasonableness of the overall rate. However, where a particular provider's costs or demand projections are far out of line with those of other providers, NECA can (and does) request clarification from that provider and it can (and does) exclude the anomalous data from the rate calculations (while notifying the Commission and the public of having done so).¹⁸⁷ Consequently, anomalies in any particular provider's data are adequately addressed by NECA so that such data does not skew the overall reasonableness of the final proposed rate. NECA's analysis and oversight obviates any need for independent public evaluation of providers' individualized cost and demand data, particularly given the potential harms that could result from the publication of such competitively-sensitive data.

Hamilton Relay has argued that the TRS Advisory Council should be provided with more disaggregated cost and demand data by the Fund Administrator.¹⁸⁸ Sorenson has expressed its support for the provision of data to the TRS Advisory Council,¹⁸⁹ but only insofar as competitively-sensitive information remains protected. Although the

¹⁸⁷ See, e.g., *2006 Rate Order* ¶ 3 (“NECA also concluded that some providers’ data was inconsistent with other providers’ data, or lacked sufficient detail, and in those cases the provider’s data was excluded in its entirety.”).

¹⁸⁸ Comments of Hamilton Relay, Inc. at 8-9 (May 17, 2006).

¹⁸⁹ Reply Comments of Sorenson Communications, Inc. at 8-9 (May 24, 2006).

Commission's rules contemplate an active role for the TRS Advisory Council, they clearly do not contemplate the disclosure of confidential data to the Council.¹⁹⁰ Indeed, the Commission's rules expressly contemplate that TRS providers – who compete against one another to provide TRS – will sit on the TRS Advisory Council.¹⁹¹ Consequently, any data that is provided to the public or to the TRS Advisory Council must be sufficiently aggregated to avoid any danger of identifying individual providers.

The utility of public analysis and comment should be balanced with the need to protect VRS providers' identifiable and commercially-sensitive information. The cost and demand information reported by VRS providers is highly sensitive. Reporting it in too granular a manner could have severe negative consequences for VRS providers and their ability to compete effectively.

The Commission has recognized the importance of maintaining sufficient aggregation of competitively-sensitive data and it has done so while reporting information in such a manner as to provide a meaningful opportunity for public analysis and comment.¹⁹² Similarly, sufficient aggregation of VRS cost data is critical to prevent competitors from identifying which costs were incurred by which providers. Furthermore, it is unclear how the provision of disaggregated data would be substantially more helpful in commenting on the reasonableness of rates than the same data supplied in a more aggregated form (*i.e.* on an industry-wide basis). In addition, the categories

¹⁹⁰ See *e.g.*, 47 C.F.R. § 64.604(c)(5)(iii)(I) (providing for the confidential treatment of providers' information and including exceptions only for administrators of other specified funds and plans – none of which include the TRS Advisory Council).

¹⁹¹ *Id.* § 64.604(c)(5)(iii)(H).

¹⁹² See *e.g.*, *Local Competition and Broadband Reporting*, Report and Order, 15 FCC Rcd 7717, ¶¶ 89, 91 (2000) (recognizing utility in aggregating data to the carrier class level to avoid individual provider identification).

proposed (*i.e.*, marketing/advertising expenses, outreach expenses, capital investment) correlate closely with a company's strategic business plans. The benefits of a competitive approach to the provision of VRS services will be diminished if competition itself is compromised through deliberate or inadvertent release of sensitive strategic information. In sum, Sorenson supports making provider data publicly available, but only in a sufficiently aggregated form so as to preclude any possibility of identifying individual providers.

X. CONCLUSION

For the reasons stated above, the Commission should adopt a new, long-term, price cap-based rate methodology for VRS and IP Relay. The Commission also should ensure that under any methodology adopted in this proceeding, the VRS and IP Relay rates remain stable for a period of at least three years, subject only to the adjustments that would occur under price caps.

Respectfully submitted,

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