Before the
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

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

To: The Commission

COMMENTS ON NECA'S PROPOSED PAYMENT FORMULAE AND FUND SIZE ESTIMATES FOR THE INTERSTATE TRS FUND FOR THE 2010-11 FUND YEAR

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TABLE OF CONTENTS

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Purple Communications, Inc. ("Purple") by counsel and pursuant to Public Notice, DA 10-761 (CGB April 30, 2010) ("Public Notice"), comments on the National Exchange Carrier Association's ("NECA") April 30, 2010 proposed Telecommunications Relay Service ("TRS") payment formulae and fund size estimates.[1] In support, the following is shown.

I. Introduction and summary.

Based on discussions with, and statements from, the staff, we understand the FCC intends to adopt TRS payment rates for an interim one-year period while it looks comprehensively at the TRS rate setting methodologies, an effort which we respectfully support. Accordingly, in this filing we will limit discussion for the most part to NECA's proposed rate submission for the 2010/2011 rate year. In summary, our discussion herein addresses the following points Purple believes are important: (1) the Commission should avoid use of a weighted average to set VRS rates because it is so weighted by the dominant 80 percent market holder, (2) we agree with the continued use of a multi-tiered rate structure; however, the Commission should expand Tier 1 and 2 to better foster competition and greater consumer choice in a dominated market, and (3)

[1] *See* Interstate Telecommunications Relay Services Fund Payment Formula and Fund Size Estimate, Docket 03-123 (April 30, 2010) ("Rate Filing").

we believe that for this interim rate period the Commission should use historical costs for determining the payment rates for Tiers, but these rates require adjustment to account for costs NECA either miscalculated or did not incorporate into the rates.

The Commission previously adopted the multi-year, three-tier rate methodology for VRS with the stated intent to promote competition within the industry by having costs for "newer providers" covered while ensuring that "the larger and more established providers will not be overcompensated." *Telecommunications Relay Services*, 22 FCC Rcd 20140, 20163, 20168 (2007) ("2007 Rate Order"). The FCC also emphasized that the methodology should "result in more predictability for the providers," and be consistent with the principle that providers are entitled to their "reasonable" actual costs of providing service. *Id*. at 20148. With a three-year period, the FCC intended providers to have the opportunity to budget their costs while having enough stability to make long-term investments and allocate funds to programs that would reduce costs in the future.

The Commission's efforts to foster competition and to provide stability and predictability over the past three years have resulted in significant advances within the industry, and allowed new and small providers to develop. The new and small providers have been leaders in advancing important consumer issues. Some of those advances include:

- The establishment of ten-digit numbering systems for relay users -- spurred by providers and consumers;
- Automatic 9-1-1 transfer and connections;
- Increased quality of video interpreting through training and operational enhancements;
- Mobile videomail;
- New video hardware and software;
- Expanded installation of video phones in businesses, workplaces and places of public accommodation;
- Functionally-equivalent features for dialing and connections.

All those advances have served to promote the Americans with Disabilities Act's mandate of narrowing the functional equivalency gap. These consumer benefits were made possible by the Commission's establishment of a stable multi-year rate methodology, and multi-tiered structure, allowing new and small providers to invest in the market and provide consumers meaningful benefits.[2]

Purple supports NECA's proposed TRS payment rates for traditional TRS, IP Relay Service and Speech to Speech Relay Service: $2.256 for interstate traditional TRS calculated using the MARS methodology; $3.1566 for STS; $1.6951 for CTS and IP CTS; and $1.2985 for IP Relay. *See* Rate Filing at 8-15. The rates calculated appear straightforward and reasonable, and the methodology appears sound. The Commission should therefore adopt these proposed rates without modification.

With respect to the rate(s) for Video Relay Services, NECA does not propose a specific rate or rate methodology; rather, it proposes several different rates based on several different rate setting methodologies from which the Commission may choose. *See* Rate Filing at 19-25. Because the different rate setting methodologies NECA proposes would have vastly different effects on the VRS industry and the ability of providers to continue to provide the public with quality service, the particular rate setting methodology the Commission chooses to implement is critical in Purple's view. In Purple's view, the VRS rate setting methodology must insure (1) functionally equivalent public service, (2) a competitive marketplace and (3) the integrity of both the VRS program and the Interstate TRS Fund.

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[2] Thus, it is Purple's intent to advocate for the Commission's continued use of a multi-tier, multi-year rate setting methodology for VRS, but to propose that additional tiers be added, and to address current deficiencies in the TRS rate setting methodology relating to allowable costs and rate of return calculation. Purple looks forward to the expeditious initiation of that proceeding.

The Bureau's Public Notice lays out key issues on which it seeks comment, specifically (1) use of single weighted averages, (2) continued use of a multi-tiered rate structure, (3) and use of historical or projected cost information. Purple will address each of these issues in these comments.

In these comments, we show that the use of a single weighted average to set VRS rates would result in the end of a competitive VRS market. Instead, we continue to support the application of a multi-tiered payment regime. With respect to the issue of historical vs. projected costs, we highlight that NECA's historical cost calculations for Tiers 1 and 2 do not substantially differ from providers' projected costs, but nevertheless appear to understate certain costs, most notably the appropriate working capital factor and 10 digit numbering costs. Accordingly, we urge the Commission for each of the tiers to adopt the NECA calculated historical cost figures but adjust them to correct for these issues. Furthermore, due to the growth of the VRS industry and the substantial decrease between Tier 2 and Tier 3 rates, it is appropriate to re-examine and enlarge Tiers 1 and 2 to avoid under compensating small and medium size providers who grow their businesses into the Tier 3 rate level. Finally, the Commission should adjust Tier 1 upward to the Tier 2 rate, plus 5 percent, to ensure that certified, small-scale VRS providers are fairly compensated and encouraged to continue to bring innovation to consumers.

II. The Commission should avoid using weighted averages to set the VRS rates.

The Commission should avoid basing VRS compensation on a single measure of weighted average costs because it can distort true costs and does not take into account critical economies of scale of the single dominant provider compared to smaller providers. Sorenson Communications, Inc., has an estimated VRS market share of approximately 80 percent. The other various VRS providers share approximately 20 percent of the market with no one provider serving more than an estimated 8 percent. So the gap between Sorenson and the rest of the market participants is substantial. Basing the VRS rate on a weighted average dominated by one provider with a market share of some 80 percent creates a false measure of true costs because much smaller providers such as Purple and the rest of the industry have significantly higher cost structures.[3] The result would be a single VRS provider, which would limit choice for consumers and remove the incentive to innovate and improve service.

III. The Commission should continue to employ a tiered rate structure for VRS.

NECA's rate filing plainly demonstrates material differences in cost between VRS providers based on their market share. Although the current method of calculating "historical" VRS costs does not capture all costs necessary to provide the service,[4] it is nevertheless clear that substantial economies of scale are present between small and medium size providers and the large dominant VRS provider.

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[3] VRS minute volumes drive a high degree of cost scalability and can support lower pricing in high volumes. Cost scalability within the VRS industry is the primary driver of cost reduction – much more so than operational productivity and efficiency. The most notable cost reduction a large provider enjoys compared to smaller providers is in the trunking efficiency which can be achieved in utilization of interpreters. The larger provider can use far fewer interpreters to handle a given amount of traffic due to the overall higher volume of calls. Moreover, it can house more interpreters per call center, saving on lease costs. In addition, a larger provider has the advantage of spreading its administrative costs over a larger revenue base. These costs include call center management, telecommunications, and indirect wages associated with executive management, legal, operations, IT, scheduling, human resources, finance and customer service. Moreover, all providers need to maintain a certain level of research and development spending; in fact there is an inverse spending relationship between minute volume and spending in order for the smaller providers to differentiate themselves and gain market share. Similarly, smaller providers require more robust sales and marketing effort to penetrate a market dominated by a near-monopolist.

[4] For example, research and development costs designed to meet currently waived standards or to otherwise improve the service provided consumers is excluded from the historical cost calculation. Similarly, the cost of providing or installing equipment necessary to access the service is excluded, despite the requirements now contained in the FCC's TRS numbering rules that providers have the capability to communicate with the consumer's equipment to provide enhanced 911 service. *See* FCC Rule §64.611(c) & (e). *See also* discussion infra at notes 5-6 and accompanying text concerning NECA's calculation of rate of return, normal internal business relay costs and 911/numbering costs.

NECA's data show that small to medium size VRS providers, each having less than ten percent of the VRS market, have "historical" costs in the six dollar range, whereas the dominant VRS provider, with a market share estimated at 80 percent, has "historical" costs of less than four dollars a minute. Having been in operating for some seven years without a fully competitive market – and using a near monopoly on video equipment to sustain its market position -- the dominant provider is able to benefit from economies of scale and to exert its market power with respect to venders and interpreters, and in servicing and marketing to a relatively "captured" audience. To enable competition in a market long-dominated by one provider, the Commission should continue the multi-tier structure commenced just three years ago. Were the Commission to adopt a single tier VRS rate – e.g., based on the weighted average costs of all providers or some other proxy -- it would invariably result in under compensating small and medium VRS providers and overcompensating the dominant VRS provider. Instead of trying to fashion a single rate for the industry, the Commission should continue the use of the multi-tiered rate system based on number of minutes of VRS processed per month, with the inquiry focusing on properly sizing the tiers and assigning the appropriate rate level to those tiers.

IV. Purple urges use of historical costs, adjusted to include costs NECA did not include in its proposed historical cost rates.

In calculating "historical" costs, NECA took a weighted average of providers' 2009 costs, and adjusted those costs up 1.6 percent for working capital, 3.2 percent for inflation and $.0083 per minute for E911 and ten-digit numbering costs. For projected costs, NECA took the information submitted by providers and reviewed the data for anomalies, discarding the data of the highest cost provider of some $10 per minute and the lower cost per minute provider of approximately $2 per minute. In each case, NECA categorized providers as in either Tier 1, Tier 2 or Tier 3 based on their average monthly minutes of VRS. *See* Rate Filing at 21-22.

Comparing the historical and projected cost figures in NECA's rate filing shows little substantial difference between the two VRS rate methodologies for Tiers 1 and 2. NECA calculated Tier 1 rates at $5.7754 using its historical methodology, and $5.7826 using provider projected cost. Rate Filing at 25. NECA calculated the Tier 2 rate at $6.0318 using historical cost and $6.1758 using projected costs. Rate Filing at 25. This is a difference of only some 2.3 percent.

NECA's calculation of proposed Tier 3 rates, however, shows a substantial difference between historical and projected methodologies. This appears explained, however, because NECA determined that the cost data the one Tier 3 provider submitted was anomalous. Specifically, this provider projected an increase in interpreter related costs of some 60 percent while forecasting an increase in VRS minutes of less than three percent. Rate Filing at 18. The result was a Tier 3 projected rate of $5.7204 compared to an historical cost rate calculation of $3.8963. Rate Filing at 25.

Purple has concerns that the historical rate calculation methodology NECA used does not fully account for all increases in costs providers experience from year to year, most notably the continuing increase in interpreter costs, and related costs such as health insurance expenses, which are rising well in excess of the 3.2 percent factor NECA used for inflation.[5] In addition, NECA's proposed 1.6 percent working capital allowance is inadequate as it is based on a 30 day

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[5] NECA's use of the 3.2 inflation rate appears to be based on nationwide salary increase data. However, due to the shortage of video interpreters, the VRS industry has experienced substantially higher wage inflation. In this vein, it is important to note that the majority of costs associated with the delivery of VRS rise substantially each year (e.g., wages, health care expenditures, rental expense). As such, if the FCC adopts historical costs as the basis for the 2010-11 interim rate, it should consider whether the multipliers NECA proposed are sufficient to cover the expected cost increases in the areas noted.

payment cycle, rather than the 65 day payment cycle actually in effect.[6] Furthermore, the allowance of $0.0083 per minute for numbering costs, from Purple's experience, is low. Purple's numbering and E911 costs are approximately $0.02 per minute.[7] Finally, it does not appear that NECA factored in the cost of normal internal business use of VRS in fashioning the historical rate proposals. In light of these issues, the historical cost figures need to be increased to correct for these deficiencies.[8]

V. ***The Commission should expand Tiers 1 and 2 to reflect the current VRS market size and to promote consumer choice and competition in a dominated market.***

When the Commission set the size of Tiers 1 and 2 in 2007, the approximate size of the VRS market was some 5,000,000 minutes of VRS per month. Tier 1 was set at 0-50,000 minutes a month or a maximum of one percent of the market, with Tier 2 set at a maximum of 500,000 minutes, some 10 percent of the then existing market. NECA projects that the VRS market for the 2010-11 rate year will increase some 60 percent to approximately 8.25 million minutes a

[6] The original 1.6 percent figure was set when NECA reimbursed providers within 30 days of month's end. In July 2009, NECA changed this payment cycle to the 15th business day of the month following the month of submission, this averages appropriately 51 days. The additional 14 days accounts for payroll cycles within the month that service is provided. In actuality then, relay providers do not receive payment for some 65 days after service is rendered. This would indicate that the 1.6 percent working capital allowance should instead be increased 3.39 percent.

[7] Purple urges NECA to submit reply comments addressing these apparent issues with its historical cost calculation methodology.

[8] Projected costs can be subject to manipulation as suggested by NECA in its Rate Filing (at 18) where it appears the Tier 3 provider projected a rise in interpreter demand in excess of 60 percent when the overall industry is expected to be relatively flat as it relates to demand projections. However, given the relative congruity between the Tier 1 and Tier 2 projected and historical cost estimates, it does not appear this has been the case with respect to Tier 1 and 2 providers. For the Tier 3 rate, it does appear the projected cost figure is unreliable due to the anomalous data provided NECA. That leaves the historical cost figure of $3.8963 as the only potentially valid cost figure. Properly adjusted to account for the issues discussed above, it would appear this figure should be adopted for 2010-11 interim rates. However, as discussed below, although that cost figure, again properly adjusted, does not appear unreasonable with respect to a provider handling some 7,000,000 VRS minutes per month, it is far from clear that this rate should be applied to a provider serving significantly fewer minutes of use per month.

month compared to the 2007-08 rate year. Given the substantial increase in the market, it is appropriate to re-examine the tier levels. It is equally appropriate to examine the size of the tiers given that NECA's historical cost rate proposal would decrease the Tier 3 rate to $3.8963 per minute, a reduction to some 62 percent from the current $6.2372 Tier 3 rate.

Purple supports NECA's efforts to construct VRS rate tier levels in accordance with the approximate costs of the providers that predominately provide service within those tiers. We also agree with NECA that not all providers operate their businesses the same way and accordingly may have different costs related to their business operations. Some providers are "resellers" whereby they do branded marketing and outreach and have regulatory responsibility for their brand, but the actual work of processing their VRS minutes is performed on their behalf by other, facilities-based, companies. Then there are facilities-based providers that operate their own networks, hire their own interpreters in addition to conducting marketing and outreach activities. For facilities-based providers, such as Purple, operating scale matters greatly to the degree of cost reduction and efficiency they may attain. In plain English, the more minutes handled and the busier are a provider's interpreters, the more efficient the business becomes because the provider is able to spread its fixed and semi-variable costs over a larger minute base. And as discussed above, administrative costs may be spread over a larger revenue base.[9]

Similarly interpreter utilization improves dramatically with scale, and as NECA shows in its rate submission, interpreter costs are the largest cost component of VRS service.[10] The lack of operating scale is why smaller providers like Purple traditionally have higher operating costs on a per minute basis than the dominant VRS provider. For the sake of consumers and a

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[9] *See* note 3, supra.

[10] Nevertheless, for the health and safety of their interpreters and the interpreting profession, and also to maintain a high level of quality, providers must limit the temptation to impose unreasonable levels of interpreter utilization on their staffs as a means to increase efficiency.

competitive market, it is vital that small providers be able to continue to provide service at a reasonable return regardless of their size.

The concern with NECA's proposal of applying the Tier 3 historical rate for minutes beyond 500,000 is that the cost break reflective in NECA's proposed historical cost rate for Tier 3, even as adjusted as we recommend herein, simply does not happen at 500,000 minutes per month. Purple currently handles between 600,000 to 700,000 VRS minutes per month, making it likely the only provider besides Sorenson that is reimbursed from within Tier 3. NECA's proposal for a Tier 3 rate of $3.8963 – even as adjusted -- at the current tier levels would negatively impact Purple and other similarly situated providers. Purple's marginal cost of providing VRS beyond minute 500,000 is well above the proposed historical Tier 3 rate. Thus, Purple would truly lose money on every minute of VRS it processes after 500,000 a month.

In this scenario, Purple -- or any other small or medium size provider -- would be dis-incented to grow its business or innovate on behalf of consumers. In fact, the optimal economic outcome under this scenario would be for a provider to limit or to shed minutes and operate its business as close to 500,000 minutes as possible. Such a scenario does not portend adequate public service because the costs of providing the service exceed the payment rate. Moreover, this scenario does nothing to promote small and medium size providers to grow their operations and become effective competitors with the dominant VRS provider. We believe a more appropriate break point between Tiers 2 and 3 would be at the 1,500,000 minute level. At this level a provider would be serving approximately 18 percent of the market and should be in a position to realize substantial economies of scale similar to the dominant provider.[11]

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[11] If the dominant provider's costs averages approximately $3.90 with a market share of some seven million minutes a month, then it stands to reason that that the break point would be found somewhere in the midpoint of that market share (say in the 35 to 65 percent levels or around 2 to 3 million) and not at the 5-8 percent levels (around 500,000). Thus, setting the Tier 2/Tier 3 breakpoint at 1,500,000 may be

In light of the above discussion, Purple encourages the Commission to adopt the following solution. We think a tiered structure makes sense and long term would advocate for an expansion of the number of tiers. For this interim rate period, however, we endorse a one-time resetting of the three tiers based on the average number of minutes handled by the industry. This would be a one-time calculation only to reset the tiers to be more reflective of the market conditions existing in 2010 vs. 2007 and the actual cost break points. Under Purple's proposed solution, using 8.25 million minutes as the current industry average per month, the tiers would be set as follows:

Tier 1: 0-100,000 minutes
Tier 2: 100,001 – 1,500,000 minutes
Tier 3: 1,500,001 and greater minutes

This approach would capture approximately 18 percent of the current market in the first two tiers. Expanding Tiers 1 and 2 in this way will allow small and medium size providers to grow to meet demand and become effective competitors with the dominant VRS provider and ultimately reach the third tier when their costs have decreased sufficiently to break even at the substantially lower break point contemplated for Tier 3.

Purple's approach is designed to be simple and sensible, given the interim nature of the rates. Adopting this approach would allow for providers like Purple to continue to be motivated to reach new customers and to innovate to the extent possible within the proposed one-year interim rate framework while the FCC considers a more comprehensive and tailored rate determination methodology.

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overly conservative. Ultimately, we do think this issue is better addressed by additional tiers, however, which would allow the breaks between tiers to be set more gradually.

VI. The Commission should increase the Tier 1 rate to encourage certified entrants and continued innovation.

NECA's Rate Filing demonstrates a logical disconnect between the rate proposals for Tiers 1 and 2. Specifically, the Tier 1 proposals are from 27 to 40 cents lower than the calculated rates (projected or historical) for Tier 2. Rate Filing at 25. The Rate Filing itself suggests an explanation for that incongruity. It suggests that the bulk of providers who fall into this first tier are not full service providers, but utilize the services of other providers for interpreting and possibly for other functions. Rate Filing at 21. This may well be true. However, Purple is concerned that a lower Tier 1 rate will serve to limit entry of additional certified competitors in the VRS marketplace and that limiting payment to only some $5.78 to providers who are not full service facilities-based providers will assure that they can never become full service VRS providers. Significantly, these providers have substantial start-up costs that the current VRS rate methodology does not allow them to expense. Accordingly, Purple suggests that the Tier 1 rate should be set higher than the Tier 2 rate. Purple's suggestion is that the Tier 1 rate for certified providers should be set at the ultimately determined Tier 2 rate, plus five percent. This would more equitably compensate providers based on their actual operations and costs of service.

VII. Conclusion.

In sum, Purple supports the continued use of the tiered rate setting methodology and opposes the use of a single weighted average proxy for the VRS rate. Because the NECA historical rate calculations would serve to under compensate providers, the Commission should adjust the historical rates to compensate. There is insufficient data to suggest that the proposed Tier 3 historical rate, properly adjusted, would be compensatory for providers serving fewer than 1,500,000 minutes a month. Thus, Purple suggests expanding Tiers 1 and 2 to cover approximately one percent and 18 percent respectively of the projected monthly VRS market. Purple also suggests adding a differential to the Tier 1 rate which would make that rate equal to the Tier 2 rate plus five percent.

Respectfully submitted,

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