August 23, 2010

Federal Communications Commission
445 Twelfth St., S.W.,
Washington, DC. 20554

In the Matter of Structure and Practices of the Video Relay Service Program – Docket No. 10-51

Re: NOTICE OF INQUIRY – Released on June 28th, 2010.

REPLY COMMENT TO SORENSON COMMUNICATIONS, INC.'S NOI COMMENT

"*Sunshine is the best disinfectant*" – Quote by Supreme Court Justice Louis Brandeis

First of all, a brief introduction; I am Todd Elliott, an ordinary Deaf citizen and VRS consumer, and I wish to reply to Sorenson Communications, Inc.'s NOI Comment ("Sorenson NOI"). I do not represent any VRS provider. I have never worked in the TRS industry. While I am NOT an economist, I do have the entrepreneurial itch in hopes of hanging my own shingle in the future. I am participating in the NOI process as a VRS stakeholder, and want to thank Sorenson Communications, Inc. for participating in the NOI process as well.

There is much to like in Sorenson's NOI comment. It essentially captures the unique economic climate of the VRS industry, which is "a competitive marketplace with homogeneous products and a high willingness of customers to switch from one provider to the other[.]"[1] It outlines the key four statutory mandates as codified in section 225 of the Communications Act, and urges the FCC "to reestablish a coherent statutory interpretation and framework[, …]by rigorously defining the meaning and scope of each of the four mandates and the manner in which each mandate will be applied to the VRS program."[2]

Next, the Sorenson NOI delves into the economic models which would be best suited for a competitive VRS industry, and aligns closely with the four key statutory mandates of the ADA;

[1] Sorenson NOI, footnote 5. In the case of the VRS industry, customers would be **consumers** as they generally do not 'pay' for the services and/or products.
[2] Sorenson NOI, page 7, Section A, 1st paragraph.

A reverse auction with multiple 'winners' or a multi-year unitary rate for all VRS providers. It then illustrates the shortcomings of the current regulatory regime of the VRS industry, using tiered rates based on historical costs in fostering a competitive marketplace for the benefit of Deaf consumers.

A. REVERSE AUCTIONS

Sorenson proposes that there is a reverse auction that would "yield several winners, none of which would have any guaranteed share of business, … [and acquire] the right to collect from the Fund as eligible providers of VRS."[3] The winners would "need to have sufficient capacity to handle demand and the need to comply with specified quality-of-service standards that would advance all four of the principal statutory mandates."[4]

Sorenson outlines the appeal of a reverse auction as applied towards the VRS industry; "would advance the four mandates of the ADA. It would preserve competition and customer choice, while eliminating the need for the Fund to subsidize a number of highly inefficient providers."[5]

A 'reverse auction' would eliminate this picture.[6] I find this troubling. Often, small (and white-label) providers come up with innovative products and services. A 'reverse auction' would severely restrict the pool of eligible providers, thereby limiting consumer choice and a lessened competitive climate in the VRS industry. Thus, I endorse the idea of having a "Provisional Certification" program championed by Convo Relay in their NOI comment.

A properly designed provisional certification program will allow certain existing white label VRS providers to remain "eligible providers" under the reverse auction process, and to

[3] Sorenson NOI, page 23, Section C, 1st paragraph.
[4] Sorenson NOI, page 23, Section C, 2nd paragraph.
[5] Sorenson NOI, pages 23-24, Section C, 3rd paragraph.
[6] Please see footnote 50, Sorenson NOI.

allow new entrants to become “eligible providers” during the time period the reverse auction is in effect. The “winners” of the reverse auction will still be subject to further competitive pressures as they know new entrants can enter the picture in this new regulatory regime.

Ultimately, as Sorenson pointed out in its NOI comment, “it may be difficult to create an auction mechanism that gives the bidders an incentive to bring prices down to the costs of the second most efficient firm, or even to the cost of a marginally excluded firm.”[7] The bigger issue is *targeting* the reimbursement rate to the second **most efficient firm** in this reverse auction. There may be regulatory burdens as the FCC tries to decide upon a reverse auction mechanism and how to structure it so that there will be multiple ‘winners’, to make this worthwhile.

B. MULTI-YEAR UNITARY REIMBURSEMENT RATE

About the ‘unitary reimbursement rate’, Sorenson proposes an alternative model in which “a forward looking cost model that would approximate the costs of a reasonably efficient provider of VRS. A well-designed forward looking cost model therefore should produce a reasonable proxy for the VRS price that would prevail in a typical competitive industry.”[8]

Moreover, Sorenson notes that a “rigorous forward-looking cost model would resolve this controversy [about large scale economies] and enable the Commission to determine whether there is any rationale for giving new entrants or smaller providers a **subsidy**.”[9]

The economic theory behind a unitary rate is sound for a “typical competitive industry”.[10] However, the *VRS industry isn’t anything but atypical*. VRS consumers do not directly pay for the service; rather, the ratepayers contribute to a Fund, and in turn, reimburse VRS providers. As Sorenson correctly points out, “VRS providers will vie for customers at the compensation rate

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[7] Sorenson NOI, page 24, 1st paragraph
[8] Sorenson NOI, pages 24-25, Section D, 1st paragraph
[9] Sorenson NOI, page 35, Section D, 2nd paragraph. Boldface emphasis mine.
[10] The FCC NOI, 67th paragraph.

set by the FCC, they will compete on the many service quality dimensions of VRS, … and as well as in their ability to locate, attract, and retain previously unserved customers."[11]

Sorenson justifies the unitary rate price reimbursement mechanism by stating that "Different firms will not be able to charge significantly different prices for the same service and stay in business […]. Instead, all firms will charge the same price or prices that very closely converge around a single price point. In the long run, that point of convergence will be a price that is sufficient to allow the **second most efficient firm** (or group of firms in the marketplace to recover the cost of providing the service."[12]

There is one major issue in setting the multi-year unitary rate reimbursement scheme for the VRS industry. It is based on the costs associated with the **second most efficient firm**. However, and it bears repeating, the *VRS industry isn't anything but atypical*. The VRS industry has one **dominant** competitor, and a cluster of lesser competitors, all vying for VRS business.

I always have held long admiration for Sorenson Communications, Inc. They were the early innovators and helped establish the vibrant VRS industry we all know and enjoy today. They have exceptionally top-notch business acumen and have brilliant business execution. They had the fortuitous foresight to manufacture and distribute videophone equipment free of charge, and to allow free point to point calls on their network at the very infancy of the VRS industry. Even today, their excellent outreach program reaches more customers and retains them, as opposed to the rest of the VRS industry reliant on "captur[ing] the business of customers currently served by other providers."[13][14]

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[11] Sorenson NOI, page 18, 1st paragraph.
[12] Sorenson NOI, pages 18-19. Boldface emphasis mine.
[13] Sorenson NOI, page 10.
[14] Moreover, other VRS companies may have shakier business plans, such relying on Deaf employees to make non-compensable calls, or being a passive billing agent for a sheer number of white label providers.

Moreover, I consider Sorenson Communications, Inc. to be the **dominant** VRS provider in the VRS industry. Ranges estimate somewhat, but competing VRS providers have claimed, albeit indirectly, that Sorenson claims 80-85% of the VRS marketshare.[15] Setting the multi-year unitary reimbursement rate to that of the second most efficient firm only serves to **enrich** the dominant firm, to the point where it is a *hidden* **subsidy** to the dominant firm.

Perhaps an illustration is warranted. Let's assume that the FCC goes with the Multi-Year Unitary Rate Reimbursement Scheme and undergoes a rigorous examination (or has a reverse auction) of all industry participants to arrive at the per-minute rate reflective of the second most efficient firm. Let's say that this comes out to $6 dollars per minute.

The dominant provider is already making a profit at $5 dollars a minute, and now is getting a subsidy of $1 per minute. [16] This dominant provider controls over 110K endpoints. Let's assume, conservatively speaking, that the average VRS use per endpoint is one minute per month. That is $110K per month, totaling up to a $1.32 million dollar subsidy per year!

Granted that was done for illustrative purposes only; I have no data or information on Sorenson and other industry participants as the previous rate-setting mechanisms have been largely kept excluded from public scrutiny. Yes, there were glimpses into the business end of the VRS industry, either through public SEC filings (Purple) or bond filings (Sorenson), or voluntary filings (Convo Relay). But, we, as the public, really don't know the whole picture.

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[15] AT&T NOI, page 5, 2nd paragraph. In page 17, 1st paragraph, AT&T alleges a single VRS provider having 80% of the market.
Sprint NOI, Page 4, last paragraph.
CSDVRS NOI, Page 18, Paragraph 15. In page 28, Paragraph 34 CSDVRS identifies the dominant provider having 90% of the equipment market. CSDVRS also alleges that the dominant provider has 100K videophones at its disposal. (Page 53, Paragraph 78)
Purple NOI, Page 6. Purple actually names Sorenson having 85% share of the VRS market and controls over 110K endpoints.
Convo NOI, Page 45, Paragraph g, NOI 69 – Structural Safeguards.

[16] For the sake of argument, I had assumed a basis point spread of 100 points, or in this case, a dollar per minute, due to the dominance as found in this equation. In Sorenson's NOI filing, they made a similar comparison involving widgets, where the better business can make them for $1 each, and competitors can only make them for $1.25 each, and the better business enjoys a potential profit of up to twenty-five cents per widget.

C. SHORTCOMINGS OF THE TIERED RATE BASED ON HISTORICAL COSTS

Sorenson criticizes the current tiered reimbursement rate regulatory regime governing the VRS industry, saying it "compensates regulated firms for the "allowable" costs they incur in providing services, it blunts privider's incentives to pursue cost-saving efficiencies."[17] About tiered rates, Sorenson continues, "flip the workings of a competitive marketplace on its head and thereby undermine efficiency."[18] Moreover, "tiered rates would be readjusted periodically to reflect the productivity gains achieved by a larger provider, they would deter any such provider from attempting to achieve such gains and would **punish** the superior business acumen of any provider that had achieved such gains."[19]

Sorenson certainly makes a **strong** case against the current regulatory scheme imposing a tiered rate reimbursement scheme reliant on historical costs for the VRS industry.[20] However, the VRS industry and its business practices are far from perfect. There are inefficiencies built-in the VRS system. There are interpreters idling by, waiting for the next call queue. There are variable costs that all VRS providers have to account for, in addition to 'sunk' costs. The vast majority of their consumers may make uncompensable point to point calls.

As a result, VRS providers resorted to shakier business plans, such as using employee calls, conference calls, international calls, consumer poaching, being a billing agent for a number of white-label providers, and/or otherwise 'gaming' the Fund. They needed the cash flow as presented in the per-minute rate to keep their businesses afloat and to attract investment capital.

However, and thanks to the FCC's February 25th, 2010 Declaratory Ruling (and resulting further reform efforts), VRS providers now have retooled their business plans and have aligned

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[17] Sorenson NOI, pages 27-28

[18] Sorenson NOI, page 31.

[19] Sorenson NOI, last bulleted point, page 31. Boldface emphasis mine.

[20] Please see Sorenson NOI, pages 26-36.

their interests in meeting the functional equivalency mandate of the ADA. A few VRS providers have gone out of business, but by large, many have stayed on and continued operating. Finally, at that point, the tiered rate reimbursement mechanism was working as envisioned by the FCC.

Now that VRS providers are no longer guaranteed to get the per-minute rate reimbursement through fraudulent, wasteful, and abusive means, they now have to analyze their business expenditures on the basis of **return of investment** (ROI). In fact, VRS providers may choose to overspend (or underspend) any compensable categories as long as it falls within their ROI guidelines in capturing compensable VRS minutes and business. VRS providers may choose to spend in categories currently not being compensated in the per-minute reimbursement rate, as long as the ROI justifies such expenses. (i.e. CPE distribution, marketing, outreach.)

Lastly, the FCC, as administrators of the Fund, has the right to enjoy the efficiency and productivity gains enjoyed by the dominant provider in the VRS industry. What may be *punishing* is *benefitting* someone else. If there is something to benefit from in this scenario, it is the ratepaying public, VRS industry and its workers, and the VRS consumers, not some anonymous hedge funds and bondholders. The dominant VRS provider is still earning substantial amounts of money, and I assume, at excellent ROI margins, at the highest tiered rates.

However, having a tiered rate reimbursement scheme, an imperfect scheme at that, for an imperfect industry sounds like a winning combination to me. It may very well be the lesser of two evils, as the prospects of implementing a unitary rate scheme may prove to be problematic. I am well aware that the Inter-Bureau Task Force on VRS Reform has a couple of economists; thanks to the adversarial nature of the NOI process, they now have better tools in reworking the per-minute compensation rate scheme ideally tailored for the VRS industry.

D. CONCLUSION.

I would like to point out footnote 82 of Sorenson's NOI comment; "The public has a right to know that subsidies of this magnitude exist, and therefore the Commission should make any such subsidy explicit and transparent in the future." I couldn't **agree** more with this sentiment. The FCC has to make transparent of any subsidies they're giving to the VRS industry, either on the low end or on the **upper end** of the VRS reimbursement rate spectrum.

Should the FCC decide to do the multi-year unitary rate reimbursement mechanism for the VRS industry, it should do so with full knowledge and implications it has for potentially subsidizing the dominant provider in the VRS market. It should do the same thing, should it maintain the status quo of tiered rates based on historical costs, making it wholly transparent.

Lastly, I **loved** what Sorenson said about VRS itself; "to eliminate discrimination by affording *all* Americans the right to functionally equivalent access to the nation's phone system. Reaffirming this fact will make clear that VRS is a **core civil right** that may not be compromised based on extra-statutory concerns, such as the size of the Interstate TRS Fund."[21] I strongly agree that having VRS is a core civil right for all Deaf Americans. However, and it truly pains me to say this, the basis of review for the NOI process should be the "*rational basis*" standard.

The VRS industry still has a long way to go and has not fully matured. There remains a shortage of qualified sign language interpreters available for community interpreting. There remain pockets of fraud, waste, misuse, and abuse still occurring in the industry. There are numerous VRS providers with questionable business models. The list goes on. The rational basis standard of review will afford the FCC tremendous flexibility during the NOI process, as it retools the entire VRS industry and makes it relevant and vibrant for 2010 and beyond.

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[21] Sorenson NOI, page 2. Boldface emphasis mine.