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

In The Matter of	)	
	)	
Structure and Practices of the Video Relay Service Program	)	CG Docket No. 10-51
	)	
Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities	)	CG Docket No. 03-123

COMMENTS OF SORENSON COMMUNICATIONS, INC.

Sorenson Communications, Inc. ("Sorenson") hereby comments on the Notice of Proposed Rulemaking ("NPRM") issued by the Federal Communications Commission ("FCC" or "Commission") related to rates and compensation for video relay service ("VRS") for the 2011-2012 Interstate Telecommunications Relay Services Fund Year.[1] The FCC poses three questions in the NPRM, and Sorenson addresses each below.

First, the NPRM seeks comment on whether it would be appropriate to extend the current rates to the 2011-12 Fund year to the extent the Commission has not completed its ongoing review of VRS rates in that timeframe.[2] Subject to the outcome of Sorenson's appeal pending before the Tenth Circuit Court of Appeals,[3] Sorenson believes that it would be appropriate to extend the current rates as the FCC proposes.

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1 *See Structure and Practices of the Video Relay Service Program*, CG Dockets No. 10-51 and 03-123, Notice of Proposed Rulemaking, FCC 11-62 (rel. Apr. 15, 2011) ("NPRM").

2 *See id.* ¶ 5.

3 *See Sorenson Commc'ns, Inc. v. FCC*, Docket Nos. 10-9536 and 10-9560 (10th Cir.).

Second, the NPRM seeks comment on the system of accounts applicable to VRS.[4] As a threshold manner, Sorenson believes this inquiry is premature, as it has no bearing on the current rates that the FCC proposes to extend and it presupposes that the longer-term rate methodology will employ a cost-of-service approach. Seeking comment on long-term accounting requirements prior to releasing an NPRM on the long-term structure of the rate methodology appears to put the cart before the horse. Unless the NPRM issued as result of the June 2010 VRS Notice of Inquiry[5] proposes to continue cost-of service regulation as the means of setting future VRS rates, there is no need for comment on this point.

More fundamentally, a cost-of-service approach is not appropriate for the VRS industry. Sorenson reiterates its position that cost-of-service regulation (that is, the regulatory approach that necessitates accounting requirements like Part 32) is counterproductive for VRS, and that the FCC should instead employ incentive-based regulation, using an auction or price-cap principles to set rates.[6] As the Commission recognized when it adopted price caps first for AT&T and then for the large ILECs, "rather than encourage socially beneficial behavior by the regulated firm, rate of return [regulation] actually discourages it."[7]

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4 *See* NPRM ¶ 3.

5 *See Structure and Practices of the Video Relay Service Program*, Notice of Inquiry, 25 FCC Rcd. 8597 (2010).

6 *See* Comments of Sorenson Communications, Inc. at 26-28, CG Docket No. 10-51 (filed Aug. 18, 2010).

7 *Policy and Rules Concerning Rates for Dominant Carriers*, Report and Order and Second Further Notice of Proposed Rulemaking, 4 FCC Rcd. 2873, 2889 ¶ 29 (1989) ("*AT&T Price Cap Order*"). The Commission explained its conclusion as follows:

> The distorted incentives created by rate of return regulation are easily illustrated. In a competitive environment, where prices are dictated by the market, a company's unit costs and profits generally are related inversely. If one goes up, the other goes down. Rate of return regulation stands this relationship on its head. Although carriers subject to such regulation are limited to earning a particular <u>percentage</u> return on investment during a fixed period, a carrier seeking to

Moreover, the accounting requirements inherent in a cost-of-service approach generate administrative complexity and expense for the Commission and providers alike as they must grapple continuously with determining what constitutes a reasonable or "allowable" cost. Recognizing this challenge and the limited tools available to address it, regulatory agencies – including the Commission – have increasingly chosen to use price-cap approaches, which provide incentives for companies to become more efficient without involving industry and regulators in extended debates about the permissibility of different categories of costs.[8]

> increase its dollar earnings often can do so merely by increasing its <u>aggregate</u> investment. In other words, under a rate of return regime, profits (i.e., dollar earnings) can go up when investment goes up. This creates a powerful incentive for carriers to 'pad' their costs, regardless of whether additional investment is necessary or efficient. And, because a carrier's operating expenses generally are recovered from ratepayers on a dollar-for-dollar basis, and do not affect shareholder profits, management has little incentive to conserve on such expenses.

Id. at 2889-90 ¶ 30 (emphasis added); *see also Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd. 6786, 6790 ¶ 30 (1990) ("*LEC Price Cap Order*") ("Unfortunately, a regulatory system that simply corrects for a tendency to pad investments or expenses is not a system that can also drive LECs to become more efficient and productive. But incentive regulation, by limiting the amount carriers can charge for their services and continually exerting downward pressure on those price ceilings, can.").

8 *See, e.g., AT&T Price Cap Order* at 2890-91 ¶¶ 31-32. The Commission explained:

> [A]dministering rate of return regulation in order to counteract these incentives is a difficult and complex process, even when done correctly and well. This is so primarily for two reasons. First, such regulation is built on the premise that a regulator can determine accurately what costs are necessary to deliver service. In practice, however, a regulator may have difficulty obtaining accurate cost information as the carrier itself is the source of nearly all information about its costs. Furthermore, no regulator has the resources to review in detail the thousands of individual business judgments a carrier makes before it decides, for example, to install a new switching system.
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> The second inherent difficulty associated with administering rate of return regulation relates to its requirement that determinations be made about how to allocate a carrier's costs among services that often are provided jointly or in common. Such determinations tend to become more economically problematic as they become more detailed. The history of this Commission's experience in this

Third, the NPRM seeks comment on how to address the cost of capital in the context of determining VRS rates.[9] Again, this inquiry appears to be premature because it presupposes that the Commission will adopt a cost-of-service approach as part of the longer-term rate methodology. Rather than seek comment on cost of capital in isolation in this NPRM, the Commission should consider it only if necessary when it seeks comment on the longer-term mechanism it eventually proposes. As explained above, however, Sorenson urges the Commission to reject any methodology that relies on a cost-of-service approach.

More fundamentally, the NPRM appears to contemplate that the Commission would declare some costs or methods of raising capital per se unreimbursable without regard to the overall results that are achieved. Sorenson submits that this approach may prove counterproductive, as it would micromanage *inputs* (specific capital costs) without focusing on *outputs* (overall rates and quality of service). Even under rate-of-return regulation, the Commission does not prescribe a capital structure, or a company's specific choice between making capital investments and incurring expenses. And under rate-of-return or any other regulatory method, the rate must be sufficient to allow a reasonably efficient firm to recover its long-run economic costs, including its debt and equity costs, which are a normal part of running any business.

Constraining the ways that companies may raise capital and incur capital costs would be especially harmful to continued investment and innovation in the VRS industry because the historical uncertainty and year-to-year volatility of compensation rates has made it difficult to

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> area over the past several decades reflects the difficulty of implementing cost allocation systems.

Id.

9 *See* NPRM ¶ 4.

raise capital. As in any business endeavor, access to capital in the VRS industry is critical to spurring innovation, bringing service improvements to consumers, and enabling providers to launch consumer-friendly offerings to differentiate themselves from each other. A rate regime that disallows compensation for the cost of raising capital will discourage further investment in VRS which, in turn, will hobble innovation and degrade the offerings available to consumers. The same is true of a rate regime that would implement "disclosure and approval requirements" related to raising capital.[10] To meet the functional equivalence requirement in Section 225(a)(3), the Commission should refrain from pursuing any regulatory approach that does not compensate providers for the cost of raising capital or that otherwise discourages investment in VRS.

Respectfully submitted,

/s/

Michael D. Maddix
Director of Government and
Regulatory Affairs
SORENSON COMMUNICATIONS, INC.
4192 South Riverboat Road
Salt Lake City, UT 84123

Christopher Wright
John Nakahata
Charles Breckinridge
WILTSHIRE & GRANNIS LLP
1200 Eighteenth Street, N.W.
Washington, D.C. 20036
T: (202) 730-1300
cwright@wiltshiregrannis.com

Counsel to Sorenson Communications, Inc.

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10 *Id.*