about changes in usage patterns and so forth, that seem to
be shifting the base away from universal service, and how
they were willing to look at that slope, and express a very
strong opinion about where it ended up; that there were no
foreseeable reversals in that slope.

I think the challenges -- you're absolutely right.
This area of regulation is full of "horse before cart-isms,"
and I think the real challenge is to see whether there are
pieces of the puzzle that you can fix and address in a way
that still leaves you the flexibility, when the next
unanticipated wave of change occurs.

We have just the benefit of a few years of
experience in the 1996 act, and already the world looks
quite different than it did in 1995 and 1996, when the act
was being finalized.

So that's really the challenge, which of these
approaches will give you or afford you the flexibility not
to have to reinvent the wheel, when the next shift in usage
trends means something additional for the base.

MR. COPPS: Thanks.

DR. GILLIS: I agree. I don't observe consensus
among the parties on how urgent the change is; although I
wouldn't expect consensus, because we are in a scenario
where change is a benefit to some parties, and not to
others, and it's difficult to get consensus on something
like that.

I would suggest that your standard ought to be obviously the act, and whether or not it's equitable or nondiscriminatory, the current issue.

But what I find the most troubling, and is probably the greatest urgency are the competitive issues. I mean, to the extent that we are dealing with a mechanism that does not support fair competition in the marketplace, you know, there is some real dollars, some real trends, some real investment, that will be affected by that.

My pet issue is sufficiency of universal circumstances, what I care passionately about, and I think that's also endangered by the current mechanism. But from a broader public policy point of view, I would put that even second.

MS. ABERNATHY: Commissioner Rowe?

MR. ROWE: Thank you. I appreciated both of your comments and your remarks concerning the importance of trying to build consensus. I think that's exactly the spirit in which this discussion was convened, and reason we're here today. That's also the reason that both of you were invited here today. So you hit the target perfectly.

I also agree, Ms. Wallman, with the importance of engaging people who are most affected. In this case, certainly, that is not limited to, but includes, the rural
carriers and their customers, and I'm pleased to have been able to do that.

Commissioner Copps asked my first question, which was, looking through the record, do you see a basis for, at least, the buds of a consensus, either as to the problem definition, or as to possible solutions? Maybe I'll leave that, unless you have any additional comments.

But then also looking at Dr. Gillis' criteria, can you, as you look through the various proposals, identify areas where some strategies may be more consistent with those criteria than with others?

DR. GILLIS: I think there are. The strategies offered are on a continuum, I supposed. They are on a continuum from modest modification as existing mechanism -- revenue based mechanism -- to a collection based approach, with the coalition's approach being probably the simplest and easiest to administer. But then with that, you have the issue that's raised by many commenters, that the IEC is not being perceived as contributing, and that being balanced against the complexity of an alternative mechanism, would allow them to contribute.

So there is a continuum, in my view, though, that there's a difference between them. I guess between your lines a bit, are there multiple feasible paths to reaching the same end; yes. Do some paths get you farther down the
road than others? I think the answer to that is yes.

My suggestion is, under the criteria outlined, focus as much as possible on the simplest mechanism you can come up with, that satisfies you that you indeed have a mechanism that complies with Section 254(d), particularly the equitable nondiscriminatory piece of that.

MS. WALLMAN: I think I'd like to kind of converse with the panels today, because the comments, although very thoughtfully reflected, often don't pick up the nuances of where the hard parts and the soft parts in the position are.

MR. ROWE: Just to keep me from running on too long, I did write out my questions for all the panelists, and I would very much appreciate seeing both of your answers to as many of those questions as you could care to address. Thank you very much.

MS. ABERNATHY: Thank you, Commissioner Rowe. I'll defer question in the interest of time, and move on to Commissioner Thompson.

COMMISSIONER THOMPSON: Thank you. I am interested in hearing both of your thoughts on this, which is that we're being asked now to advise the FCC on making adjustment. It's a number of years after the act has passed. During those years, we've seen dramatic changes in the way communication services are delivered to consumers. How important do each of you think it is for us to
design some kind of mechanism that's going to withstand the
next series of changes; or, in deference to the idea
expressed by Ms. Wallman, of being aware of folks' anxiety
in making dramatic changes, should we be doing something
that is implemented in a series of small and repeated
changes? How do you balance the need for stability and
certainty in the markets, with the need to implement a
policy that folks can live with?

MS. WALLMAN: I think that's an important
statement to the competing interests that need to be
balanced. There's always a tension in policymaking about
incremental change versus big picture change. I think that
this is a case where you know sort of what the trend lines
are. We have some opinions -- not always do opinions agree
with each other -- but opinions about where the trend lines
go.

Do people think there's going to be a reversal in
the trend about interstate minutes? Well, probably not --
as people learn to use other technologies to communicate
over longer distances. It probably will continue in the
same direction.

So it would seem to me that if you base your
decision based on known trends, you end up putting the
system on at least a glide path. The Commission, and I know
many state commissions, have a lot of experience with glide
31 path type approaches to solving problems, where you don’t
start at the 10th story of the building and jump all the way
to the first.

You construct a system that is based on triggers.
You know you need to get from ten to one, and you have a
series of triggers over time, that adjust with what’s
happening in the market. So that might be a way to bridge
the two extremes.

MS. ABERNATHY: Do you have any comments?

DR. GILLIS: Well, I generally agree with Ms.
Wallman’s statement on that. I think incrementalism has its
assets and value. That’s generally my philosophy on the way
I would approach these types of issues.

In this particular case, however, I wouldn’t rule
out a more dramatic jump to the end, if you can conclude
from your own investigation of the issue, that you’re
comfortable that one, the current mechanism is broke, if
that’s a conclusion that you choose to make; and secondly,
that one of the options on the table that’s being offered is
adequate and really gets you to a mechanism more consistent
for the world that we live in now.

The reason I say that is, it kind of goes back to
my opening comments. It’s that I see this mechanism as a
foundation piece that needs to be set aside, if possible, so
that you all can focus on the merits of sufficiency issues,
and non-competitive reform issues.

To the extent this mechanism is something that’s sitting out there, that’s imperfect, and if you can fix it, it’s still going to be an issue in proceedings. So if you can set it aside, it’s great. But that really depends on your comfort level with the information that you have, to make those changes.

MS. ABERNATHY: Commissioner Jaber?

MS. JABER: Thank you, Chairman.

Ms. Wallman, if I heard you correctly, you said through your work on the consumer education counsel, you were able to run some models, or the group was able to run some models, and determine what the impact of the per-connection methodology was?

Can you share some of that information with us; if not necessarily today, but can you file it in the record in this proceeding, so that we could have access to those numbers?

MS. WALLMAN: I’d be happy to do that. The work was, in large part, to the credit of Joe Luben of AT&T, who spent some time to run some numbers.

MS. JABER: Thank you.

MS. ABERNATHY: Commissioner Martin?

MR. MARTIN: Thank you.

I wanted to follow up on the same kind of
questions that I think Chairman Thompson was asking regarding the balance between taking some immediate steps, and also trying to address the longer term potential issues.

I think I understood you as saying that certainly, to the maximum extent possible, when you can put an issue to bed, that’s the better approach, to resolve it and put it on the side.

But I also heard, in the initial comments, about the importance of trying to reach consensus on the issues, on the longer term approaches.

To further complicate it, in talking about the urgency of acting in some way on something now, particularly, I think you mentioned, Dr. Gillis, the urgency of the competitive issues; vis-a-vis, the competitive issues that have been raised in some of the technology neutral issues.

I found it interesting, your most recent comment, Kathy, about the fact that we could have triggering points along the way.

Would you consider that being maybe an appropriate step, where we would actually try to address some of those competitive issues and/or consumer confusion issues; and at the same time, make a recommendation along the lines of what would be a triggering point, so to speak, that it would show that those changes were insufficient to address the long-
term problem, and then it should automatically have some other solutions be put in place? Is that like what you were talking about, when you were talking about triggering points?

MS. WALLMAN: Potentially so and, you know, I would like to reflect on that approach a little bit, an flesh it out, before saying too much more about it.

But on the consumer confusion issues, just to be specific, the thing that I think really wastes a lot of time and causes a lot of pain in prior efforts surrounding universal service was the blame game that ensured afterwards about, you know, whose charge is this; who gets blamed for it; what do we call it?

If we could put that aside and get out of the business of, you know, adding to consumer confusion by making it even more confused about why it happened, I think that would -- if we just take that head-on, I think that would be a huge contribution to the stability of the system.

MR. MARTIN: And actually along those lines, if we were able to address maybe that issue, and get out of the blame game, so to speak, and be able to take on that issue head-on, and potentially have at least an initial addressing of some of the competitive issues, do you think that actually might release some of the pressure in the system, and allow for a more thoughtful and/or consensus building
approach to the long-term issues that are being raised, from the technological standpoint?

MS. WALLMAN: Possibly, but the best shot you have, I think, at getting people comfortable with stepping away from the blame game is that you have a change you need to announce. So if you’re not solving that problem, then you may not have the leverage to get people to agree on what to call it and how to explain it.

MR. MARTIN: Thank you.

MS. ABERNATHY: Commissioner Dunleavy?

MR. DUNLEAVY: Thank you, Madam Chairman.

I generally share the concerns that everyone has expressed, given the complexity of the issue. Minimizing consumer confusion and, in an incremental way, getting to where we have to go is one way, or some dramatic change.

Do you have any thoughts -- I’m not quite sure I understand the difference and distinction between consensus and compromise, if we’re trying to get this. Isn’t there a need for that? Isn’t there a need for compromise, in order to get to a consensus where you have so many opposing views?

MS. WALLMAN: I think that people will have to give things up, but what I’m suggesting is, compromise is a process that’s more in control of the parties. They sort of decide what they are willing to live with, and present it to the decision-makers, and try to get it ratified.
I think that this process, unfortunately, is going to be more difficult than messy or good than that approach would allow. Consensus building is usually a time consuming process.

For better or worse, I think that’s going to be a significant consumption of time for the next little while; where the members of this Board try to bring out the best in each of these proposals, to figure out what is useful to you in constructing a solution, and telling people what they’re going to have to give up, and what they’re going to have to live with. So that’s the distinction I’m able to draw, between consensus building and compromise.

DR. GILLIS: I think the point that I was trying to make on consensus is partly a pragmatic caution, in that this is an issue that consensus, at least in my view, would be very difficult to achieve, because of its complexity. Consensus is always a great help, when we can get it.

But what I worry about most is that the mechanism itself should not be a barrier to making other important decisions that you all need to make. That consensus is also needed on those decisions, as well.

So if you can really put this issue behind you, the issue of the mechanism itself, even if it requires some hard decisions, and hard decisions based on your reading of the law, I guess that’s what it comes down to. Then that
will help you later on, in getting more consensus on issues that could involve expansion of universal service, if that were needed, or issues that might involve competition in areas served by rural carriers, from the state commission standpoint.

So it's just a tough issue, and it's one that I, personally, don't hold out that much hope that you are going to receive full consensus on. That obviously means airing your views and listing, and finding it common ground, if possible. I'm not as optimistic about that.

MS. ABERNATHY: Thank you, Dr. Gillis; thank you, Ms. Wallman -- if you have the chance to stay around and offer some closing thoughts at the end, based upon what all of the witnesses say, that would be helpful, I think. So thank you again, and we'll move on to the next panel.

Once again, thanks to everyone for coming today, and helping us grapple with these very difficult issues. Panel one, as we mentioned, is really the contribution assessment methodologies, and discussion by each of the parties about the proposals they have pending in front of us.

I think the easiest way to do it is simply start with John Nakahata, work our way down, and we'll let all of the presentations be made. Just be sure when you start talking, first of all, be mindful of the time. We really do
I want to hear from all of you. And the other point is, when you start, be sure and state not just your name, but who you are representing and some of your background, before you get into the details of your presentation.

So John, if you’d like to start, that would be great.

MR. NAKAHATA: Thank you, Commissioners, and I apologize in advance. I managed to come down with a cold today. So I’ll try and speak directly into the mike, and I apologize if I cough.

My name is John Nakahata. I’m here representing the Coalition for Sustainable Universal Service, which is made of up AT&T, WorldCom, and -- Telecommunications Users Committee, and level three. We’re pleased to present testimony this afternoon.

We obviously have put forward the connections based proposal in probably its most straightforward and simple form, and we would urge you today to act on that as soon as possible, and we would really hope it would be in time for implementation in January.

There are five points I want to make to you today. Point number one, the current system is broken, and it can’t be fixed. We’ve seen an unprecedented decline in interstate telecommunications revenues over the last two years, and
with that unprecedented decline in interstate switching access minutes.

That's significant, because that's never happened before, since the FCC started keeping statistics in 1984. We've had recessions in that time period since 1984, and we've never seen this happen before. Something deeper is going on, and it's systemic. It just can't be fixed by adding, for instance, to the wireless safe harbor, because there's something else going on, too, and that's bundling.

There's no way that a revenue based system can handle bundling; not when you have bundling of interstate and intrastate, and bundling of telecommunications and non-telecommunications services, which is the way that services are procured now in the business market, and increasingly is the way that services are provided in the residential market, as we've seen with the introduction of the MCI neighborhood plan. There's no way to assign dollars in a bundle consistently.

If you have got to go with an alternative, then what's the best alternative? COSAS is the most competitive alternative proposal we've got. It charges the same fee to people providing similar competing services to the same end user customer.

SBC Bell South's proposal does, by contrast, look at competitively neutral on its face, when it would not be
competitively neutral in its application. I’ll explain that
a little more in my next point, which goes to the issue of
transactions costs and administrative costs.

The COSAS proposal is the simplest and most
efficient solution. It minimizes transaction costs by
focusing on a single collection point. I’ll us again, SBC
Bell South -- not to pick on Judy -- but I’ll use SBC Bell
South as a contrast, which is, it maximizes the number of
collection points that you have.

It means that for the ordinary residential
consumer, there may be as many as three or more providers of
service that have to collect the data you need to run
universal service, to bill and collect those connection
fees.

That’s inefficient. It’s also inefficient because
the ILAC, or the connection providers, are the only ones who
are going to have the information needed to run that type of
connection based system, on the order of SBC Bell South.

IXCs and ISPs will have to buy that information
from the ILECs. That’s an additional cost in the system.

It’s totally unnecessary. There’s no competitive reason
that we need to have it.

The fourth point that I want to leave with you is,
the COSAS proposal really does reduce the average
residential USF fees across all income groups. I have
provided the members a chart that tries to compare the
current system in the COSAS proposal and SBC Bell South.
You'll notice that SBC Bell South is significantly higher,
and does not relate at all to the carrier mark-ups.

The last point I want to make is obviously the
law. We do believe that the COSAS proposal is legal, when
you read that within the confines of 254(d). With 254(d),
you have to read it though in its entirely, both all of its
sentences and all of it clauses.

The first sentence says, "Every telecommunications
carrier that provides interstate telecommunications services
shall contribute on an equitable and nondiscriminatory
basis." That means, first and foremost, you have to have an
equitable and nondiscriminatory basis, or you don't get out
of the starting gate. That basis then has to get applied to
every telecommunications carrier. We think we do that.

Then what happens if that number is small or
nothing? If the number is small or nothing, then the
Commission can exempt that carrier from paying under its
diminimus authority, and this dis-harmonizes all three
portions of 254(d).

I mean, the key, again, is, is it equitable and
nondiscriminatory? I think one example, except for the
premise that the COSAS proposal is equitable and
nondiscriminatory, if you were to read every
telecommunications carrier as saying, literally that you had
to generate a fee, you could have a proposal that said,
well, we'll take the COSAS proposal, but if it is a zero,
we're going to assign a charge of $1.

But the $1 would still be diminimus. That's sort
of reading the act to require a lot of gymnastics, that we
don't think is really necessary. It's much more
straightforward, just reading it as deductible,
nondiscriminatory, and you apply it to every carrier. If
the amount is low, the carrier can be exempt and is
diminimus.

In short, we think that this is the most
straightforward, most efficient, most sustainable way to
move forward, and we urge the Commission to adopt it.

MS. ABERNATHY: Thank you. I'm sorry about your
cold.

MR. NAKAMATA: I apologize.

MS. ABERNATHY: We won't ask a lot of questions,
that way, of you.

MR. NAKAMATA: I'd be happy to answer whatever
questions you have.

MS. ABERNATHY: Ms. Walsh?

MS. WALLMAN: My name is Judy Walsh. As many of
you on the panel know, I am a recovering regulator --

(Laughter.)
MS. WALLMAN: -- having served on the Texas
commission for a number of years, before taking my current
position with SBC Communications as Senior Vice President of
State Regulatory Compliance.

You know, we most of the time think about SBC as
an ILEC. But we really operate as an IXE and a CLEC, and a
broad band service provider and an ISP, and through the
joint venture with Bell South, as Cingular Wireless, which
the nation's second largest wireless carrier.

So I think that puts us in a bit of unique
position to think about and make recommendations on how
universal service should be reformed and how the funding
assessment should be made.

There is an opportunity for consensus, I think, in
that the Congress, this Commission, and all the state
commissions have always valued the right of every American
to have telecommunication service, and have it available on
a four wheel basis.

This is a long-recognized public benefit, and I
don't think there's any question but what it's one that we
all continue to value.

The real question then becomes about the funding.
And it's also clear that the cost of universal service is
very significant. It, I believe, is estimated to go to $6.2
billion this year, and a lot of experts say that we'll
continue to rise in the future.

So while no one questions the public benefit, it's also irrefutable that the level of these charges is a pretty good burden on providers, and it isn't always seen as value added by the customers.

So the question of how to implement a new plan is done in the light of providers who are paying and customers who are paying and would like to reduce their charges; and those who are not paying, who would prefer not to pay. So the challenge is to come up with something that works in that context.

The Commission has identified a number of issues with the -- of the current mechanism, and I agree that this one can't be fixed. We've already talking about the shrinking revenue, and I won't go into that.

But I think equally as important is that the current system is not able to adjust to changes in the marketplace -- CLEX is entering the local market; RBOC entering the long distance market; substitution of wireless for traditional wire line and long distance; and also the transition over to Internet telephony.

It is not competitively neutral or technology transparent, because you look at DSL contributing a cable modem, not LEX and IECs contribution IP telephony.

Packaging and service bundling are not easily accommodated
in the current plan, and there is clearly a lack of uniform recovery that confuses customers, and makes them question the legitimacy of the charges on their bills -- all of which are problematic in the current system.

I think as you explore proposals to reform this system, the real challenge is to make sure that customers and providers perceive that the charges are equitably imposed. I think this requires that any opportunities for arbitrage, for any gaming tactics that shift charges among customer classes, are eliminated; and that similar services are assessed in the same manner, regardless of technology or regulatory treatment of the provider.

I think if we can come up with a plan that meets those goals, we probably will be able to build consensus around some of these issues.

The SBC Bell South plan develops a comprehensive proposal to reform the current system. I believe the proposal represents a fair and equitable approach to solving many of the problems that the Commission has identified.

Under the plan, universal service support would come from interstate telecommunications activity involving end users. This means that every provider of telecommunications, regardless of technology platform or facilities ownership, ILECs, CLECs, IXCs, wireless operators, paging companies, private carriers, cable modem
operators, ISPs and other content providers, would contribute, based on the retail services it sells to end users, as long as that service incorporates an interstate telecommunications component. These would be qualifying services.

When the end user purchases a service from a provider, they purchase the right to connect to the network, and to receive service at some specified bandwidth level. This is a qualifying service connection.

All interstate transmission will be composed of an access connection and an interstate transport connection. An end user could establish multiple retain relations, or they could purchase an integrated or bundled service from the single provider. In either case, the amount of the assessment is the same, if a service is the same.

The question of whether the universal service charge appears on a single bill, or more than one bill, depends on the customer’s choice. They can choose multiple providers or not.

The more the customer purchases, the more they contribute to universal service; and the more bandwidth they purchase, the more they contribute to universal service.

The plan satisfies a threshold of the statute, in that every telecommunications carrier that provides
interstate telecommunications services will contribute. And the act doesn’t say, provider of access or connection. It refers to services; and long distance service clearly is an interstate service.

It broadens the contribution base to ensure viability and stability. It’s not regressive, because contributions are based on the services the customer purchases. It’s nondiscriminatory, because comparable services have comparable funding. There are no cost subsidies, and it does eliminate the lag issue, which has been problematic for carriers.

So I believe that this proposal does resolve the majority of the problems in equitable way, and I appreciate very much being able to participate.

MS. ABERNATHY: Thank you, Ms. Walsh.

Okay, Mr. Nishi?

MR. NISHI: Good afternoon, and thank you for inviting me here today. I’m pleased to be before you today. As you said, I’m Roger Nishi, and I’m the Vice President of Industry Relations for Waitsfield-Fayston Telephone Company in Vermont.

I’m also here today representing El Pasco, the nation for the promotion and advancement of small telecommunications companies.

I’m honored to be here to discuss this very

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important subject with you. I would also like to take the
time to thank you for making this time available in your
very busy schedules. I know many of you probably had plans
for a Friday afternoon, heading out for the weekend, and
this may be taking the place of that. So I do thank you for
being here.

I really want express my passion for the industry.
Communications is a great thing. My son, he’s five years
old, and he thinks it’s magic. That’s probably because I
told him so.

(Laughter.)

MR. NISHI: But it is a wondrous thing.
I have a passion for rural telecommunications and
what it does for customers in rural areas of the U.S. We
have brought advanced services to rural customers for years,
oftimes in much quicker fashion than the larger
companies, and that’s key.

At Waitsfield, we make sure our customers aren’t
left technologically behind the more urban areas. All these
are very important. Because of this, our customers are
better off and our communities are better off. So we think
we are doing a good thing.

But what’s been the key to all of this? Universal
services has been a big, big portion, and has allowed us to
bring many of these technologies to our areas.
The Commission’s universal service policies have been key to rolling out services in a timely manner, at rates comparable to those in urban areas. Universal service funding mechanisms have helped to advance the technologies in rural high cost areas.

Waitsfield’s customers have benefitted from this. It’s not easy serving mountains and places where there’s lots of rocks; areas where people don’t live in population clusters.

We always say and we joke about this all the time, if the -- if the cows had phones, it would be much cheaper to provide services to urban areas, as we would have some population densities; but it’s not going to happen.

So today, I sit here consumed by universal service. I’m concerned as to whether the current system is sustainable; whether there will be sufficient funding in the future. More customers -- overall high cost areas continue to receive the benefits of universal service funding. I hope so.

I guess what we’re here today to do is to try to determine what we can do to establish an equitable amount of discriminatory contribution system, that provides for specific predictable sufficient funding, to preserve advanced universal service.

In this light, I would like to talk about

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contributions a bit. El Pasco is in agreement with the FCC goals in this proceeding, to ensure the stability and sufficiency of the fund, as the marketplace evolves; to assess contributions in an equitable and nondiscriminatory manner; and to provide certain -- participants -- to delay costs of compliance.

El Pasco is supportive of the Commission’s exploring a flat fee working contribution assessment. With that, I have four points that I would like to make.

Point one, any flat monthly contribution assessment mechanism must require an equitable nondiscriminatory share of contributions from more than one interstate carrier. That includes -- local exchange carriers. That includes inter-exchange carriers, SRECs, and anybody who does carry an interstate type of service.

Legally, Section 254(d) states that any telecommunication carrier that provides interstate service communications shall contribute an unequitable amount on a nondiscriminatory basis. It’s the law, so we feel that should be upheld.

As you are aware, two days ago, the Senate Subcommittee held hearings on universal service. There appeared to be an overriding them from that, in that they believe income-based mechanism could only buy companies with end users, is both illegal and not fair.