

Time Warner Proposal

**biography of presenter
executive summary of proposal
written testimony**

Susan M. Baldwin, a Vice President for Economics and Technology, Inc. (ETI), has worked nineteen years in public policy, thirteen of which have been in telecommunications. She is an expert in diverse telecommunications areas including universal service, cost proxy models, numbering issues, alternative regulation, network modernization, local exchange competition, cost methodology, and rate design. (ETI specializes in telecommunications economics, regulation, and public policy.) Ms. Baldwin has participated in numerous state and federal telecommunications policy proceedings, has testified as an expert witness before state regulatory commissions, and has served as an advisor to several state regulatory commissions and consumer advocates. Ms. Baldwin served four years as the Director of the Telecommunications Division for the Massachusetts Department of Public Utilities, where she advised and drafted decisions for the Commission in numerous proceedings and directed a staff of nine. In addition, Ms. Baldwin has worked with local, state, and federal officials on energy, environmental, budget, and welfare issues. [Master of Public Policy, Harvard University's John F. Kennedy School of Government; Bachelor of Arts, Mathematics and English, Wellesley College, nominee, Rhodes Scholar.]

**EXECUTIVE SUMMARY OF TIME WARNER COMMUNICATIONS
HOLDINGS INC. COMMENTS REGARDING UNIVERSAL SERVICE
METHODOLOGY; CC DOCKET NOS. 96-45, 97-160, DA 98-715**

Wherever possible, the FCC should avoid subsidizing rates in rural, insular and high cost areas where cost-based rates are affordable. This policy approach comports with Section 254(b)(1) and sound policy. Wealth transfers to consumers with relatively high incomes advance absolutely no identifiable social goal.

In a paper submitted in this proceeding, "Defining the Universal Service 'Affordability' Requirement: A Proposal for Considering Community Income As a Factor in Universal Service Support" ("ETI Study"), Economics and Technology, Inc. ("ETI") quantifies the harm in not recognizing that consumers in the top 30 percent income bracket can easily afford cost-based rates. The ETI Study analyzes average income by census block group ("CBG") in conjunction with cost model results to determine universal service funding requirements in high-cost, high-income areas. It demonstrates that approximately 20-30% of the high-cost universal service fund could be eliminated if support were limited to households with incomes below the 70th income percentile. This could result in up to \$4.5 billion in savings nationally.

Thus, the FCC should work toward eliminating federal universal service funding for CBGs with average median incomes above an appropriate threshold, for example the 70th percentile. The elimination of these subsidies will of course result in lower compensation for the carrier serving these high-cost areas. In many states, incumbent LECs do not have the flexibility to raise rates to account for the elimination of the federal subsidy. A state could respond to this problem either by gradually phasing in cost-based rates to avoid rate shock (the preferred outcome) or by increasing the state subsidy to make up for the loss of federal funds. In any event, the decision to subsidize high-income areas should be made by and paid for by the states. In addition, as the ETI Study acknowledges, certain consumers in a particular high income CBG may not have the ability to pay cost-based local telephone rates without serious difficulty. Accordingly, where a state has transitioned to cost-based rates, it may be necessary to establish a "safety net" for those consumers. Finally, the FCC should consider establishing a cost-based local service "cap" beyond which all costs would be subsidized at the federal level, so as to avoid any consumer shouldering an extraordinarily burdensome monthly local telephone bill.

**FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

**EN BANC HEARING ON
PROPOSALS TO REVISE THE METHODOLOGY FOR
DETERMINING UNIVERSAL SERVICE SUPPORT**

CC Docket Nos. 96-45 and 97-160

STATEMENT OF SUSAN M. BALDWIN

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on behalf of

Time Warner Communications Holdings Inc.

June 8, 1998

STATEMENT OF SUSAN M. BALDWIN

I am Susan M. Baldwin, Senior Vice President of Economics and Technology, Inc. ETI is a consulting firm specializing in telecommunications economics, regulation, management and public policy. I was a principal author of the paper, *Defining the Universal Service "Affordability" Requirement*, that forms the basis for Time Warner Communications' proposal to the FCC for consideration of community income as a factor in universal service support.

ETI's analysis of the relationship between income and high-cost support was an outgrowth of our detailed analyses of various cost proxy models that were first presented to the Commission in 1996, in the early stages of CC Docket 96-45. One thing that struck us was the fact that the models that purported to "target" support on the basis of high-cost also directed support to many well-to-do communities where customers clearly could afford to pay for the entire cost of their local telephone service, without any subsidy whatsoever. Further research demonstrated that this was not an isolated condition; it was a nationwide pattern. ETI's analysis demonstrated that a decision not to fund support to high-income CBGs would result in a significant reduction in the overall size of the interstate high-cost fund.

The *Telecommunications Act of 1996* explicitly requires that "affordability" be included as a consideration in the development of a comprehensive universal service support mechanism: "Quality and rates — Quality services should be available at just, reasonable, and *affordable* rates." The extent to which service is "affordable" to an individual consumer is inextricably tied to that consumer's income level and ability to pay, and in fact the Joint Board, in its Recommended Decision, and the Commission, in its Report and Order, have acknowledged that income level directly affects the determination of what is an "affordable" price. The Commission has also agreed that community income, as represented by the percentage of students eligible for school lunches, is a valid basis for establishing the variable discounts necessary to make telecommunications affordable to schools and libraries.

The universal service goal is not advanced by subsidizing consumers who can afford to pay the entire cost of their telephone service — and whose decision to take service is unaffected by the presence of such a subsidy. Indeed, some of the specific attributes of exclusive high-income communities — large lots, low population density, remoteness from primary population centers — are the very same conditions that tend to raise the cost of providing local telephone service. Ironically, many low-income areas, such as densely populated inner-city communities, are because of such attributes also *low-cost* areas, and could well be forced to subsidize the “high rent” high-cost-to-serve suburbs.

Policies that would flow universal service support to such communities serve only to impose significant costs and economic burdens upon other segments of the economy while doing nothing to advance the cause of universal service or produce any other offsetting economic or social benefit. Among other things, a funding obligation that is larger than one that is minimally necessary to achieve the universal service goal will undermine other Commission and Congressional objectives, perhaps even including universal service itself! By forcing new entrants to make larger-than-necessary payments to the universal service funding mechanism, such policies will increase the costs of and barriers to competitive entry, and thereby diminish the prospects for effective competition overall. They will also work to suppress demand for price-elastic services, thereby limiting the potential benefits that all sectors of the economy can derive from increased access to and use of the nation's telecommunications resources.

The ETI study and Time Warner's proposal are not offered as providing definitive or prescriptive guidance as to how to structure an income-based funding mechanism. Rather, it is offered to demonstrate

- that many “high-cost” communities are also high-income communities;
- that public data is available from the Census Bureau to support the administration of a community income-based funding mechanism; and

- that there is an opportunity to achieve a significant decrease in the overall size of the universal service support fund, fully consistent with the statutory requirement that service be "affordable," without any consequential impact upon the overall universal service goal.

The structure of a community income-based funding mechanism should be built upon three specific policy initiatives:

- *First*, the FCC and the states should conclude that the highest income high-cost areas are to be excluded from universal service support. For example, if all CBGs with median income levels in the top 30% of their state were placed in this category, the funding requirement could be reduced by as much as 20% to 30%. The specific policy can be highly flexible, and can involve state-specific or national income standards, or some combination, as well as absolute and/or flexible affordability thresholds.
- *Second*, there should be a safety net for low-income consumers residing within high-income high-cost areas who cannot afford to pay full cost-based rates.
- *Third*, to avoid rate shock, transition plans should be established that would allow carriers to move rates in high-cost high-income areas toward their full forward-looking costs.

If done correctly — and it can be done correctly — the result will be "win-win" for all concerned: Universal service at affordable rates can be assured, while minimizing the potential adverse impact upon nascent competition, innovation, and the economy generally.

Thank you very much for the opportunity to present these comments here today.