Remarks of Thomas L. Welch, Chairman of the Maine Public Utilities Commission
March 6, 1998

Chairman Kennard, members of the Commission:

Good Morning.

As Chairman Kennard recently stated, there is no fundamental inconsistency between the Act's dual objectives of preserving and enhancing universal service, and of creating effective competition in all telecommunications markets. Competition will ensure that this country remains at the forefront of innovation and capital formation; universal service will ensure that the benefits of competition are realized by all our citizens.

For universal service to be achieved in fully competitive markets, however, the current framework for assisting high cost areas of the country is inadequate and should be replaced. Moreover, I believe that the proposal contained in the Commission's May 8, 1997 order -- generally referred to as the 25/75 approach -- fails to address the fact that, without sufficient direct support for basic rates, the rates for customers in some areas will be neither affordable nor reasonably comparable to the rates available in urban areas.

Let me describe both the nature of the problem and the outlines of a possible solution.

There are many states where the number of customers served in high cost areas is so large, relative to the number of customers served in low cost areas, that if left entirely to its own resources a state would have to impose enormous surcharges on its low-cost customers to bring its high cost customers within hailing distance of either comparability or affordability.

A comparison of two states, California and Vermont, illustrates the problem. In both states, the cost per line, measured on a forward looking basis, is roughly the same for each density zone. For example, where the density is from 5 to 100 customers per square mile, the costs in both California and Vermont are a bit over $40 per line. Where the density is over 10,000 customers per square mile, the costs for both states are around $10. But there is no similarity between California and Vermont when you measure the proportion of lines within each density category. In California, fewer than 5% of the lines are in the 5 to 100 density zone; in Vermont, about 30% are in such sparsely populated areas. On the other hand, in California more than 30% of customers live in areas where there are more than 10,000 line per square mile; Vermont has only about 5% of its customers in such typically low cost areas. Unlike California, Vermont simply does not have enough low cost lines to offset the higher cost lines and reach a balance that is consistent with the Act.

The existing system for distributing support to high cost areas cannot reasonably coexist with a competitive market because, among other things, the amount of support available to an entrant, or to an incumbent, would depend upon the characteristics of the incumbent -- for example, whether it serves more or fewer than 200,000 lines. In the old days of implicit subsidies, it may have been expedient to differentiate among carriers based upon their size: where subsidies must be explicit and portable, such distinctions are untenable.

The 25/75 approach likewise falls short. First, by directing support to reducing interstate access rates, the proposal fails to provide any federal support at all for local rates for customers living in high cost areas: that obligation would fall entirely to the states. Second, because this approach would fund only 25% of the need, states with a disproportionate number of customers who live in high cost areas will simply be unable to meet their burden without vastly distorting the rates that must be charged to customers in their relatively few low cost areas.

There is, however, another way. Chairman Kennard has articulated the purpose of a federal high cost fund as a "safety net." I suggest that net should come into play where states cannot, by virtue of their geographic characteristics and the distribution of their populations, generate for themselves enough support to ensure that all their citizens enjoy basic telecommunications services at rates that satisfy the Act's standards for affordability and comparability.

Put another way, the amount of federal support available to any state would be limited to the amount needed by that state **that exceeds the amount that the state can raise from within its own borders by balancing its own low and high cost areas.** The amount of federal support thus would assume that each state has "taken care of its own." This approach expressly recognizes that the universal service obligation of the Act is appropriately shared by the state commissions and the FCC.

The proposal accompanying these remarks (a slightly revised version of an *ex parte* submission filed on February 10 by the commissions of Maine, New York and Vermont) outlines an approach that may serve as a useful model for reform of the high cost fund. The proposal grew from efforts by state commissioners representing a broad range of interests to see if we could find common ground. We recognized that any sound approach should be consistent with the needs of competition, provide sufficient support to satisfy the comparable rate standard of the Act, and would necessarily involve significant compromise by all of us. While we continue to work to refine the proposal, I believe that it represents a fair and balanced model that could serve effectively as we move into the uncharted waters of local competition.

We do not have the time this morning for a full recitation of the proposal. In broad outline, federal support would be given only where a state's average costs, measured by the lesser of embedded or forward looking costs, exceeded the national average. The proposal also includes provisions to ensure that carriers and their customers who receive support under the existing system are not placed at a disadvantage. We estimate the proposal would result in only a modest increase in the overall level of high cost funding, and thus, in our view, would keep the fund at a level that does not impede the growth of competition.

The states, including Maine and its rural counterparts, are committed to opening our markets and bringing the benefits of competition promised by the Act to our citizens. We are just as committed to finding a way to be sure that the telecommunications needs of our citizens who live in areas that are costly to serve are met at affordable rates that are comparable to the rates available to their more concentrated brethren. I encourage you to consider the approach I have outlined today.

Thank you for the opportunity to meet with you this morning.