TELECOMMUNICATIONS INDUSTRY TRENDS AND REGULATORY CHALLENGES

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INDUSTRY TRENDS

- Growing competition: all sectors
- Revenue growth limited by price competition
- Substitution/sector growth differences
  - Wireless and broadband/data are growth markets
  - Voice stable or declining
  - Access lines declining
    - Wireless substitution
    - Competition-CLECs, cable
    - Broadband
  - Access minutes declining more rapidly than access lines
    - Wireless substitution
    - email
INDUSTRY TRENDS

• Bundling---leading to product integration
  – Standalone long distance declining (especially in consumer market)
  – Bundle penetration increasing—local/ld/broadband/wireless
  – Integration of services (e.g., wireless/wireline) beginning

• Packetization/VOIP
  – Drivers of packetization
    • Efficiencies
    • New product/feature opportunities
  – Voice becoming just another data application

• Trends are leading to a redefinition of the market and the industry
  – Traditional categories of carriers and services becoming obsolete
SPRINT STRATEGY IN A CHANGING INDUSTRY

• Positioned across all sectors
  – ILEC, wireless, long distance, CLEC, data, voice

• Transformation (initiated in 2004)
  – Customer-facing Organization (rather than organizing around products)
    • Sprint Business Solutions (wireless and wireline)
    • Sprint Consumer Solutions (wireless and wireline)
    • Sprint Local Consumer Solutions (ILEC operations)
    • Integration of systems and network
  – Objective: Integration of services—not just bundling
  – Customer service—”table stakes”
    • Companies that don’t provide superior customer service will be at a significant competitive disadvantage
REGULATORY CHALLENGES

• Traditional regulatory “boxes” increasingly out of sync with the marketplace
  – State/interstate
  – Voice/data
  – Local/toll
  – Wireless/wireline
  – Cable/telco
  – information service/telecom service

• Industry evolution driving a fundamental reevaluation of the regulatory framework
INTER-CARRIER COMPENSATION

• Access (long distance) and reciprocal compensation (local)
  – Over $10 billion a year
• System full of inconsistencies, contradictions
  – And huge incentive for arbitrage
• Rate structure differences
  – Access: compensation paid on originating and terminating
  – Reciprocal compensation: paid for termination
INTER-CARRIER COMPENSATION

• Rate level differences
  – Interstate access: .6 cents per minute of use (mou)—large ILECs
  – State access: 2.4 cents per mou (average)
    • Lows: e.g., WY at .9 cents per mou
    • Highs: e.g., some companies in AZ at 15 cents, NM at 18 cents per mou
    • Florida is one of few states to tackle the issue of state and interstate access rate disparity
  – Reciprocal compensation rate
    • .07 cents per mou (for most companies)
INTER-CARRIER COMPENSATION

• Carrier differences: wireless
  – MTA local calling area
    • Gainesville to Jacksonville call
      – Local if wireless
      – Long distance (access) if wireline
    • Pensecola to New Orleans—local call
  – Wireless pays but doesn’t receive access
    • Example: Gainesville to Atlanta call
      – Wireless to wireline: access paid to wireline carrier
      – Wireline to wireless: no access paid to wireless carrier
INTER-CARRIER COMPENSATION

• Carrier differences: ISP bound
  – Carriers with ISP bound in 1Q 2001: recip comp (on 2001 mou)
  – Carriers with ISP bound after 1Q: bill and keep

• Access exemption
  – Enhanced or information services

• VOIP access rules—don’t exist
  – AT&T petition: VOIP anywhere in call stream—no access
    • How much VOIP is required to qualify for access exemption—1 foot, 1 mile, etc.?
INTER-CARRIER COMPENSATION

• Enormous industry/regulatory/legal resources expended in policing the system
  – PIUs, PLUs, intra-MTA factors, etc

• Need to get to unified inter-carrier compensation system ASAP
  – Compensation the same regardless of:
    • Jurisdiction
    • Carrier classification
    • Information or telecom service
    • Technology
VOIP

- VOIP—not just the public Internet
  - Private networks as well
- Access issue should not be allowed to obscure the larger issues
- Wide variety of flavors of VOIP—don’t all fit in one regulatory box
  - Technology replacement in traditional network
  - Computer to phone over broadband
    - Cable
    - But also Vonage (core vs edge)
  - Computer to computer over public Internet
VOIP issues

• Public safety: E911, CALEA
  – Legitimate concern
• Economic regulation: tariffs, service quality, billing, etc.
  – Less need for all carriers as competition evolves
• Rights of VOIP providers should not be lost sight of
  – Interconnection
  – Numbers
  – UNEs
• Need framework that doesn’t stifle or retard development of new services—not unique to VOIP
  – Wireless/wireline integration poses same issues
• But also protects rights of VOIP to essential capabilities
USF

• Another broken system
  – $6.5 b fund today
  – Pressures to grow
    • Rural USF—wireless
    • Inter-carrier comp reform likely to require further USF
  – Funding base
    • Interstate retail revenue:
      – not growing
      – Difficult to measure in integrated product world
    • Inequitable
      – Traditional IXCs shoulder most of the burden
      – Cable modem vs DSL
      – VOIP implications—can they avoid USF as well as access?
USF

• Efforts to constrain fund
  – Rural USF: for rural companies only
    • Rural customers of non-rural ILECs not “in the system”
  – Proposals to limit USF to “primary line”
  – Resistance to USF for wireless carriers

• Need to rationalize USF funding
  – Broaden the base by assessing telephone numbers
    • Technology/service neutral
    • Doesn’t depend on ultimate legal classification of VOIP

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