

## Members of this Committee

My name is Everett M. Ehrlich. I am the President of ESC Company, an economics and business consulting practice located in the Washington, D.C. metropolitan area. Prior to founding ESC in 1997, I served as Under Secretary of Commerce for Economic Affairs under Commerce Secretaries Ron Brown, Mickey Kantor, and Bill Daley, as Chief Economist and Vice-President for Strategic Planning of Unisys Corporation, located in Blue Bell, and as Assistant Director of the Congressional Budget Office for Natural Resources and Commerce.

Let me also note that Verizon Corporation is a client of ESC Company, but that it has not dictated the content of this testimony, which reflects my own professional views.

I appreciate the opportunity to submit my testimony regarding HB 1608, to amend Title 66 of the Pennsylvania Consolidated Statutes and modernize the regulation of communications. In my testimony today, I will first discuss the general issues we face in the contemporary communications sector, and then the particulars of HB 1608 and how they address those issues.

There is a saying in the game of baseball that goes like this: "You can't steal second with one foot on first." This is precisely the situation we face in communications, and the reason why this bill addresses an important problem.

In 1934, a national framework for telecommunications policy was adopted by the Congress in the Communications Act of that year, which established the basic structure of communications for the next half-century. There would be a sanctioned monopoly for this industry that provided universal and reliable service in exchange for a regulated rate of return. The long distance market would be serviced by AT&T – Ma Bell – and the states would sanction local carriers – the largest of them the Bell operating companies – that would interconnect with the national system. They would settle up their financial claims under the eye of regulators. The FCC, which was created in the 1934 Act, would regulate the prices of interstate calls, and the states would regulate the local end of the system, including the provision of basic local service, which is what we're discussing today.

This arrangement allowed for a variety of social policies, including the ability to use cross-subsidies (for example, charging a higher price for inter- and intra-state long distance) to make local dial tone cheaper than it would have been - usually below cost.

But the same system had disadvantages as well. Most importantly, it virtually prohibited innovation. If the Bell system didn't make the equipment, you couldn't use it, and if they didn't want to connect with a competitive provider, they wouldn't. And that became the system's undoing, because technology can't be held back, even if regulators want it to be so. It soon became possible for companies other than AT&T to provide long-distance calling using microwaves, and cable systems could do the job the copper wires of the local carriers did. Mobile phones proliferated rapidly once spectrum was allocated to them (and once they were

freed from state regulation in 1993). And when the Internet became a household affair in the mid-1990s, it brought VOIP and other services into the picture. All of these new technologies competed with the analogue, copper-wire system, and all of them challenged the basic assumption behind the old system – that we were better off with one, regulated monopoly system than a competitive market.

So the policy set out back in 1934 changed, first by the Courts approving the restructuring of the industry in 1984, and then by the Telecommunications Act of 1996, which itself was spurred by reform in some states. The new national policy laid out in that Act welcomed and encouraged competition in telecommunications, and competition has spread like gangbusters. I recall, as a child, being lined up with my siblings and cousins to speak to relatives a few hundred miles away on Sunday night, in order to use the expensive phone time efficiently. Today, we talk to anyone, anywhere, using any methods, without a second thought. And as opposed to a “dumb” phone that was only good for connecting to the system, the devices we use not only allow us to talk, text, and send messages, but to have access to the entire Internet and the full range of services and experiences it offers.

But, as I said earlier, while we’re rapidly moving into this new era, we still have vestiges of the old one – we’re racing to second base but still have one foot on first. This is the problem that brings us here. In essence, the old system imposed burdens on the companies that provided copper wires to our home because some kind of control was necessary in the absence of competition. These burdens made sense when the regulated local phone company was the only provider of service. But now that competition is here and customers have many options, these regulations, which fall on only the legacy carriers, are unnecessary and harmful.

Here’s a telling example of what I’m talking about. We all look enviously at Google’s decision to invest in a one-gigabit network in Kansas City – doesn’t each member of this Committee wish Google had made such a commitment to their own district? But the Google Kansas City fiber system will not offer voice service, even though the cost of delivering voice packets is virtually nothing. Why? Because, if they did, as one Google executive said, “there are all of these special rules that apply.”

Think about that – if Google won’t deliver voice services on a custom-made, state-of-the-art network, then what are the incumbent phone companies going through? They’re competing with one hand behind their back. That’s bad for them, of course, but more importantly, it’s bad for all of us. It means that they have fewer resources available to invest in the infrastructure that brings us new technologies and other innovations. It means that the state will offer a poorer telecommunications environment to businesses when compared to other states that get the picture. It means that the incumbent companies have to jump through regulatory hoops that were designed for the monopoly era in terms of reporting, regulatory permissions, and investment decisions that delay improvements and add to cost. And we get nothing out of all that wasted effort and expenditure.

This is a situation that calls for a remedy but, at the same time, the remedy should provide assurances during the transition to people who are reluctant to see changes regarding their phone service, as well as those who value important services provided by phone, such as first responder access. And there should be a standard by which those relatively few markets or individuals who do not have as many choices in the new world of digital telecommunications can transition at a more gradual pace.

Fortunately, in my view, H.B. 1608 anticipated and addresses all of these issues. As I read the bill, it recognizes the robust competition already in place in non-rural communities (as defined by population density), while maintaining regulatory protections in rural markets where the pace of change is not as fast.

Even consumers in these “competitive” areas would still be entitled to important protections. Consumers will continue to have access to basic calling services, including 911 access, at competitive prices. The existing phone company would also be obliged to continue to offer basic service to all of its customers for at least four more years regardless of the situation in that market. And if there are households in these competitive areas that are not served by a company other than the existing phone company, they can petition the Public Utility Commission to keep their service going.

Consumers in rural areas will have these and more protections under the bill. Most importantly, rural communities can only be designated as competitive if phone service is provided by three separate providers, one of which is a landline. If that condition is not met, that area will stay in the old regulatory system. And before a rural area can be designated a “competitive,” its provider must satisfy the Chapter 30 obligations to bring broadband to that area. The bill also requires the PUC to look into the Pennsylvania Universal Service Fund and implement any changes by 2019, while demanding greater transparency and targeting in its disbursements in the meantime. This provision provides important certainties to the rural carriers in these times of rapid industry change.

It should also be noted that this legislation would not change any of the other aspects of telephone service. The PUC would still oversee service standards related to the safety, reliability, termination and restoration of telephone services in non-competitive markets. All carriers would continue to have to provide Lifeline service. The point of this bill is not to roll back these protections, but to assure that all carriers satisfy them equally, and completely.

So, in my view, this bill strikes the right balance between modernizing the state’s telecommunications infrastructure while protecting consumers and respecting their right to be served. Consumer rights are important and will be assured under the bill. High-speed communications networks are important, too, and are vital to Pennsylvania’s economy. This bill will improve the investment climate for these networks.

All sectors of our economy rely on the flow of information and depend on communications networks. Thanks to ongoing investments in voice and data infrastructure, the so-called “old

line” telecommunications companies and others are competing to bring us the networks of the future. But we need policies that let Pennsylvania attract more of this investment. Unfortunately, many of the current rules in the wireline local communications industry were designed decades ago and now apply to only a small group of the State’s communications providers, without providing any meaningful benefit to most of our state’s citizens.

HB 1608 will give Pennsylvania an opportunity to modernize – but not rashly eliminate -- the state’s outdated regulatory environment, while ensuring that rural Pennsylvanians continue to have access to basic calling service. It is a reasoned and balanced approach to a problem that has been allowed to linger too long. We do not have to choose between technological change that produces jobs and growth, on the one hand, and the rights of our citizens to basic services they have known all their lives. We can have both, as this bill demonstrates. A strong, bipartisan effort to pass this bill will signal to the telecommunications industry that Pennsylvania is prepared to embrace change and the broadband future that awaits us all.