



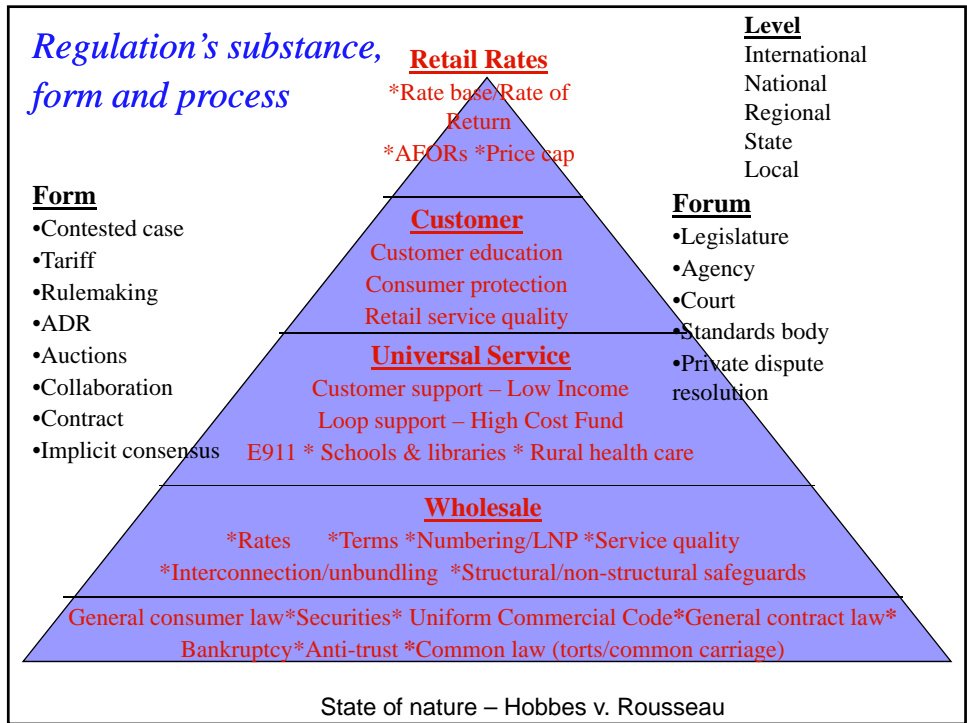
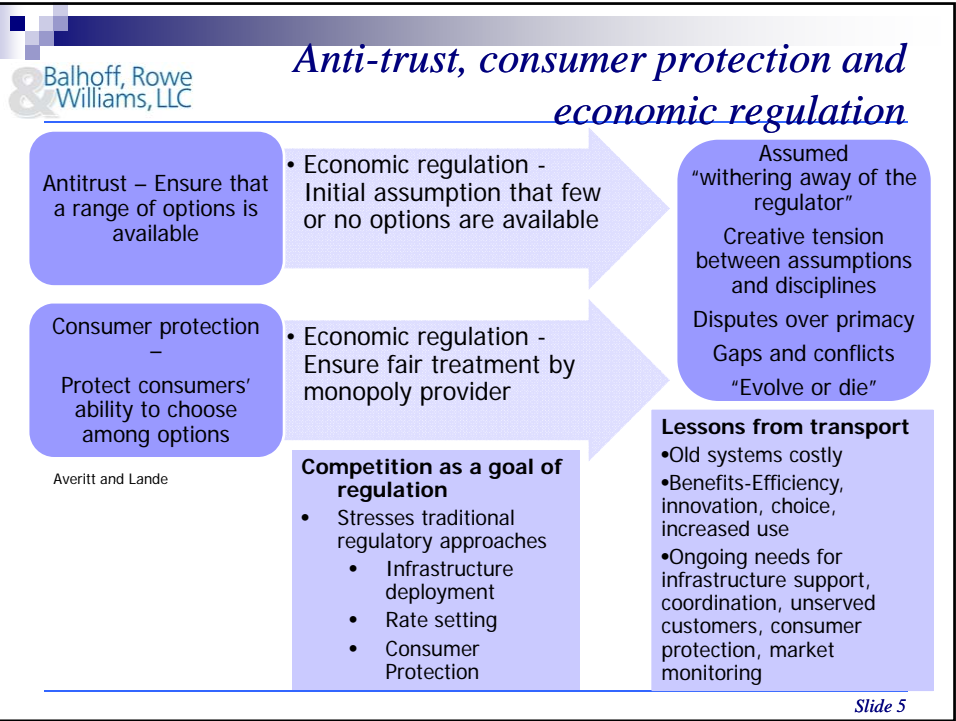
 Balhoff, Rowe  
& Williams, LLC

*CITI*  
*The State of Telecom 2007*  
*Regulatory evolution and*  
*approaches*

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- Anti-trust, consumer protection and economic regulation
- European and U.S. approaches
- Competitive disruption of traditional regulatory tools
- Concluding questions

*Anti-trust, consumer  
protection, and economic  
regulation*



## *European and U.S. approaches*

### Balhoff, Rowe & Williams, LLC *European Union reform goals*

- EU review of 2002 telecoms rules, commenced in late 2005
- Goal of “future proof” rules recognizing convergence of digital technologies
  - Remove bottlenecks to “faster, more innovative and competitive services”
- Emphases
  - Market-oriented deregulation
  - Focus on ex-ante approaches
  - Streamline regulation
  - Spectrum – flexibility, simplification, coordination
- Specifics
  - Reduced roaming rates
  - One-stop regulatory shopping
  - Reject German “regulatory holiday” for broadband –
    - Endorse evolution from service to infrastructure competition
- Concluding extended consultation, proposals due November 13 2007

## EU – U.S. comparisons

Subsidiarity	Federalism
More activist competition policy – appears more consistent with “structure, conduct, performance”	Less activist anti-trust Appears tempered by “public choice”/“law and economics”
Refusal to forbear for broadband – rejects national “regulatory holidays”	“Title I” reclassification of broadband
Formal structure driven by market definition, findings of Significant Market Power	Gradual partial decoupling of sector from economic regulation Increasingly focused interventions, including support for Carrier of Last Resort
Infrastructure: Wireline + <i>unbundling</i> + wireless	Infrastructure: Wireline + <i>cable</i> + wireless
Estimated 20% broadband infrastructure competition	Estimated 80% U.S. broadband competition
Currently higher European broadband deployment	Currently higher US wireline cap ex/revenues
European Regulator’s Group	NARUC

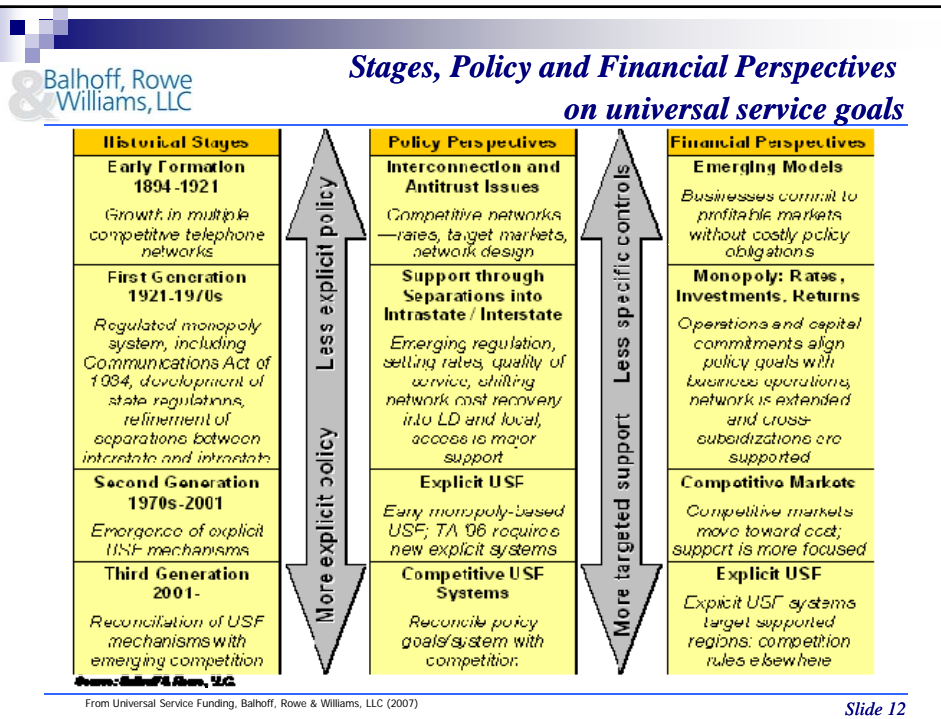
## Themes and variations

- Interplay of anti-trust (ex post) and economic regulation (ex ante)
- Monopoly – competition continuum
- Temporal dimension
- Gaps and inconsistencies
- Jurisdictional tensions and resolutions
  - Approaches to federalism and subsidiarity
  - U.S. Commerce clause
- Litigiousness
  - “Lawyers behaving badly”?
- Universal service
  - Consistent goals over time, pursued through varying/evolving means
- Investment and deployment concerns
- Disruptive effects of technology and economic models on then-current regulatory regimes
- Different approaches to and assumptions about consumer desires and consumer protections

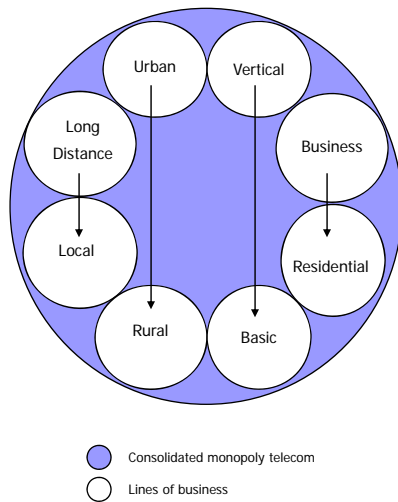
## Competitive disruption of traditional regulatory tools

Implicit versus explicit support of high cost areas, customers, services

From *Universal Service Funding*, Balhoff, Rowe & Williams, LLC (2007)



## Monopoly Model of Support

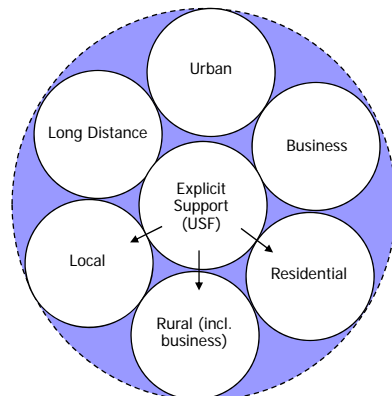


- Policymakers regulate carriers to ensure policy-based ubiquitous/affordable services in exchange for economic viability of entire enterprise
- Historically, residential and high-cost rural consumers benefited from a system of enterprise-based internal cross-subsidies
  - Support included in access and long distance
  - Geographic rate averaging
  - Value-of-service pricing
  - Residual pricing of value added/"vertical" services
  - Rate differentials unrelated to cost differences
- System began to fail when certain sources (lines of business) of internal cross-subsidies became competitive
  - LD from approximately 1970
  - Business in the 1990s/2000s
  - Residential with VoIP in 2000s

From Universal Service Funding, Balhoff, Rowe & Williams, LLC (2007)

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## Competitive Model



- Explicit support mechanisms intended to eliminate internal cross-subsidies
  - Access systems
  - Federal/state USF programs
  - Access reforms
- Competition targets most profitable business lines, eroding profitability & making cross-subsidies unsustainable
  - LD market example
- All lines of business must be economically justifiable
  - Allow competition to govern competitive markets
  - Uneconomic regions receive increasingly explicit support
  - Policy support matches policy duties

From Universal Service Funding, Balhoff, Rowe & Williams, LLC (2007)

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## Concluding questions

Balhoff, Rowe  
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### Traditional and evolving policy roles

Function	Needed or not?	Who does it and how?
Retail rate setting		
Carrier of last resort		
Wholesale structure, rates, terms		
Enforcement		
Mediation and facilitation		
Organization and system management		
Information to facilitate choice		
Consumer protection		
Infrastructure support		
Others		

*Which functions are needed? How are they best performed? By whom? Coordination? Do some conflict?*

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- Diverse business models allow comparisons
  - Is broadband a separate network?
  - Approaches to COLR and rural
  - Implications for regulation and policy
  - AT&T is once again the largest local and long distance company in America – and the largest rural carrier
- Meaningful cross platform competition
  - CATV providers are offering telephony services
  - Strong and rapid success
  - Tend to focus on dense areas, but includes smaller towns as well as larger cities
- Video products
  - IPTV- the ability to deliver television content via IP over broadband facilities
  - Verizon's FIOS roll-out compared to DSL-based deployments
  - Most telcos using last mile copper
  - Need to address backbone networks as well
  - Telcos are attempting to get content deals from the media companies
- Transactions
  - Sales of rural properties
  - Wireline spins
  - Roll ups of smaller companies
- Spectrum!

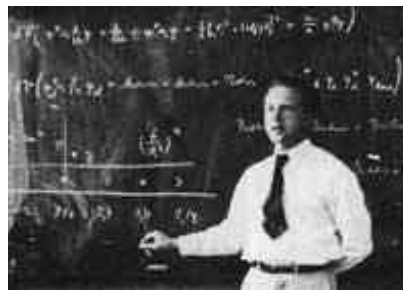
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*"One cannot simultaneously find both the position and momentum of an object to arbitrary accuracy."*

-The uncertainty principle

*"Policy solutions tend to look simple from a distance, and messily complicated up close."*

- Regulatory corollary



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## About Balhoff, Rowe & Williams

Balhoff, Rowe & Williams, LLC is a specialized professional services firm focused on providing financial-regulatory advice. The principals have more than 40 years of experience in advising investors and regulators on complex investment issues. They have provided services to a wide range of communications companies, including incumbents, competitive carriers, wireless operators and cable operators. Additionally, the firm has expertise in energy and other utility services. The services of Balhoff, Rowe & Williams include research, think-tank projects, professional facilitation, advocacy efforts, financial and restructuring advice for various companies, carriers and policymakers. The company offers an unparalleled combination of experience, credibility, strategic insight and access in a rapidly changing environment.

### **Michael J. Balhoff, CFA, Managing Partner**

Michael J. Balhoff, CFA, is managing partner at Balhoff, Rowe, & Williams LLC. Previously, Mr. Balhoff headed for 16 years the Telecommunications Equity Research Group at Legg Mason, which advised investors about equities in media, cable, wireless, telephony, communications equipment and regulation. Prior to joining Legg Mason in 1989, Mr. Balhoff taught at both the graduate and undergraduate levels. He has a doctorate in Canon Law and four master's degrees, including an M.B.A., concentration in finance, from the University of Maryland. A Chartered Financial Analyst and a member of the Baltimore Security Analysts Society, Mr. Balhoff has been named on six occasions as a *Wall Street Journal* All-Star Analyst for his telecommunications recommendations. His coverage of telecom was named by *Institutional Investor* as the top telecommunications boutique in the country in 2003. He has also testified multiple times before congressional committees, is regularly a featured speaker at conferences for investors and policymakers, and is widely quoted in the media, including television, newspapers as well as communications and business journals.

### **Robert C. Rowe, Esq., Senior Partner**

Robert C. Rowe, Esq., is a senior partner at Balhoff, Rowe & Williams LLC. Previously, Mr. Rowe served as the Chairman of the Montana Public Service Commission which was responsible for regulating telecommunications, electricity, natural gas, water, and some transportation services. Mr. Rowe also served as President of the National Association of Regulatory Utility Commissioners, Chairman of the NARUC Telecommunications Committee, member and state chair of the Federal-State Joint Board on Universal Service, member of the Federal-State Joint Conference on Advanced Services, chairman of the thirteen state Operations Support Systems Collaborative working with Qwest and its competitors to achieve compliance with Section 271 of the 1996 Federal Telecommunications Act, and member of various advisory boards for university-affiliated programs.

### **Bradley P. Williams, Esq., Partner**

Bradley P. Williams joined Balhoff, Rowe & Williams as a principal in 2005 and became a Partner in 2007. Previously, Mr. Williams was a member of the Strategic Planning & Business Development group at Lowe's Companies Inc., the Fortune 50 home improvement retailer. Prior to joining Lowe's, Brad worked with Mr. Balhoff in the award-winning Telecommunications Equity Research Group at Legg Mason, focusing on incumbent and rural local exchange carriers. Prior to joining Legg Mason, Brad was a co-founder of eSprocket / Beachfire, a venture-backed company that evolved into one of the pioneers in mediation technology solutions for the financial services sector. Previously, he served as a financial executive for Iron Road Railways Incorporated, a Washington, D.C.-based holding company that integrated, through acquisitions, a significant regional freight rail network serving northern New England and eastern Canada. Brad began his career as an investment banker in First Union's Capital Markets Group. He has a BA in Economics from the University of North Carolina and a JD from the University of North Carolina School of Law.

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