Telco
Fiber Fiascos:
Will Accelerated Infrastructure Programs Be the Next Nuclear Power Plant Debacles?

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What caused the nuclear power plant debacles?

State regulators were induced to believe promises of technological miracles: energy "too cheap to meter".

In the end, for example, New York's Shoreham, Pennsylvania's Limerick, New Hampshire's Seabrook and others were among the most expensive, useless investments ever made. Once construction started, and the costs soared, regulators were locked into billions of cost overruns. Only environmental dangers ended this hemorrhage. In many cases, not a kilowatt of commercial energy ever was produced. Shareholders and ratepayers both lost fortunes.

What are telephone companies doing?

Telephone companies are playing a similar game. Their promise: technologically sophisticated broadband telecommunications services to every home, and basic telephone service "too cheap to matter".

Where's the flaw in this promise?

How do the telephone companies propose to make the "field of dreams" come true? The answer is enormous demand -- mass market demand -- for the new services that are made possible by the new investment. But that's the danger: if only a few users really want the new services, how can the services be priced low enough so that the mass of consumers can afford them without some sort of massive subsidy? And if the great mass of consumers don't take the new services (because they don't want them or can't afford them), how will the revenue from new services subsidize low basic telephone (dial tone) prices?
Why should states resist the temptation to play the telcos' game?

Because the risk is too high: there is no apparent mass market demand for any sophisticated new telecommunications services.

For example, independent surveys of consumers show little if any interest in any new "information" or entertainment services that could be delivered over wire or cable to the home. Without mass market demand, basic telephone services and ordinary consumers will end up subsidizing telephone companies' unnecessary investment and the exotic new services used by a few large businesses and up-scale households. At the same time, other companies that could do a better job of matching specialized demand with investment will be discouraged from investing in a state's public telecommunications infrastructure.

Thus, rather than promoting economic development, improved education and better health care, a policy bias toward the incumbent monopoly and a "field of dreams" will burden the state's economy (remember the nuclear plants?) and divert scarce resources from the traditional but still vital industrial infrastructure, schools and health care facilities.

What are the telcos proposing?

A typical proposal is to place fiber cable to every home by some date in the next century and to freeze residential telephone rates for a few years, provided there is less regulation and the oversight on the telco.
Isn’t that good... freezing rates?

No, it is an illusionary benefit at best and a consumer rip-off at worst. Telephone rates are probably already much too high compared to declining costs so that a “freeze” denies to consumers the rate reductions they deserve. Telcos will divert the consumer’s rate reductions into their “field of dreams”: the fiber network for which there is no obvious residential consumer need. But the same network -- paid for by residential subscribers’ forgone rate reductions -- will be used to provide sophisticated business services at very low prices. This is nothing more than consumers being forced to subsidize the telcos’ ability to preempt competition in business markets.

Even if a telco is required to share with ratepayers earnings over a particular level (12-14% is typical), allowing such a high level in today’s capital markets gives the company opportunity for a huge windfall during the period it is using ratepayer funds to pay for unneeded facilities.

After the “rate freeze”, basic rates could soar: the expensive fiber optic investment will have to be paid for, and its undepreciated book value will mean huge basic service rate increases, unless usage for new services, like video-on-demand, reaches astronomical heights. How many households are likely to spend hundreds or even thousands of dollars each year when they have been unwilling to pay a small extra charge for touchtone service, call waiting, and call forwarding?

How efficient will the telco fiber investment be?

Because telephone company investors will not be placing any of their own capital at risk, the telephone company will not be constrained to invest efficiently. (Consumers will be forced to make the investment through forgone rate reductions.) Overall, ratepayers will pay more under these circumstances than they would if competitors were permitted to supply facilities, too.
Is there a more sound, less risky approach to fiber deployment?

Yes, New York is a good example of a better approach. That's why New York's telecommunications system is so far ahead of its neighboring states that are continually dependent on the telcos. New York's policy of encouraging market forces to provide infrastructure and encourage innovative new services has fostered the most robust public telecommunications network and the widest array of choices in the country.

- New York's infrastructure is dynamically appropriate to users' evolving needs and pocketbooks.
- New York State is currently served by a multitude of diverse carriers, all of whom are investing in and developing New York's advanced telecommunications infrastructure under the discipline of a competitive market rather than under the largess of a monopoly service provider.

Other states such as Illinois, Massachusetts and Michigan have policies that encourage competitive infrastructure deployment and those states have also seen the beneficial results of these progressive policies.

Who benefits from a competitively deployed infrastructure?

Everyone:

- Residential consumers and small businesses immediately get lower rates (or slower increases) and improved quality and reliability as a result of the telephone company's overall network efficiencies and improvements induced by the limited competition for special business services. In the longer run, all consumers can have similar choices, if a state's pro-competitive policy is continued.

- Telecommunications-dependent businesses that are the backbone of an "Information Age" economy have the operational security (route and switch redundancy, vendor diversity, self-healing networks, and the highest level of reliability) they need to grow. The improved services installed for businesses are widely available to educational and health care facilities.

- The telecommunications industry will be healthier and more profitable. Competition forces incumbent telephone companies to be efficient and to focus on what they do best, helping to ensure their long-term success, while competitors serve markets that telephone companies cannot serve or do not serve well.
Who pays for “advanced services” in a competitive infrastructure?

Users of advanced service pay the cost of the facilities they use: general ratepayers are not forced to pay for things they don’t want, need or benefit from. The need for monopoly investments leading to expensive cross-subsidies is minimized, and the long-term revenue requirement for the basic services is minimized.

What is the best way to continue a low-risk, pro-consumer infrastructure policy?

A number of actions by State government will help:

- **Initiate, support and expand a competition policy at the public utility commission**, particularly with respect to the interconnections and interoperability required to establish a consumer-friendly “network of networks”.

- **Use government to generate demand, not subsidize or manage supply**. The State and municipal Governments, educational institutions and medical institutions can use existing budgets to improve their own productivity through telecommunications, and various vendors can bid to supply the facilities.

- **Ensure universal service** -- the availability of a basic level of modern telecommunications services to all citizens -- through a new Universal Service Assurance policy that targets subsidies only to individuals that need the assistance. All suppliers of local telephone service should have an equal opportunity to compete for the subsidies so that every citizen can enjoy the quality, service and innovations spurred by competition. By targeting the subsidies and allowing carriers to compete for the subsidy, the size of the subsidy will be reduced.

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