The seal of the Office of Regulatory Staff, South Carolina, is a circular emblem. It features a central image of a palmetto tree, which is the state tree of South Carolina. The tree is set against a background of a rising sun or moon. The words "OFFICE OF REGULATORY STAFF" are written in a circular path around the top of the seal, and "SOUTH CAROLINA" is written around the bottom. In the center, over the tree, are the large letters "ORS".

# **Annual Report**

## **The Status of Local Telephone Competition in South Carolina**

Compiled by  
The Office of Regulatory Staff

2008

Table of Contents

**Introduction..... 3**

**Local Exchange Market ..... 3**

    Incumbent Local Exchange Carriers..... 6

    Competitive Local Exchange Carriers ..... 6

**Telecommunications Service Pricing ..... 10**

**Wireless Carriers ..... 12**

**Broadband Deployment ..... 14**

**Consumer Services..... 17**

**Regulatory Landscape ..... 18**

**Conclusion ..... 19**

## **Introduction**

In order to track the changes occurring in the telecommunications industry, the Office of Regulatory Staff (ORS) has been directed by the South Carolina General Assembly (SC Code Ann. Section 58-9-280 amended by Act 318 of 2006) to compile information and monitor the status of local telephone competition in the state on an annual basis. The purpose of this document is to report the status of competition in the local telephone exchange market in South Carolina, to note any major changes that have occurred in the marketplace, and to monitor the effect of broadband and wireless services on the competitive local exchange market. This is the third report compiled by the ORS pertaining to this information. Statistics are included to help readers understand the local telecommunications market, the carriers, and their market share in South Carolina.

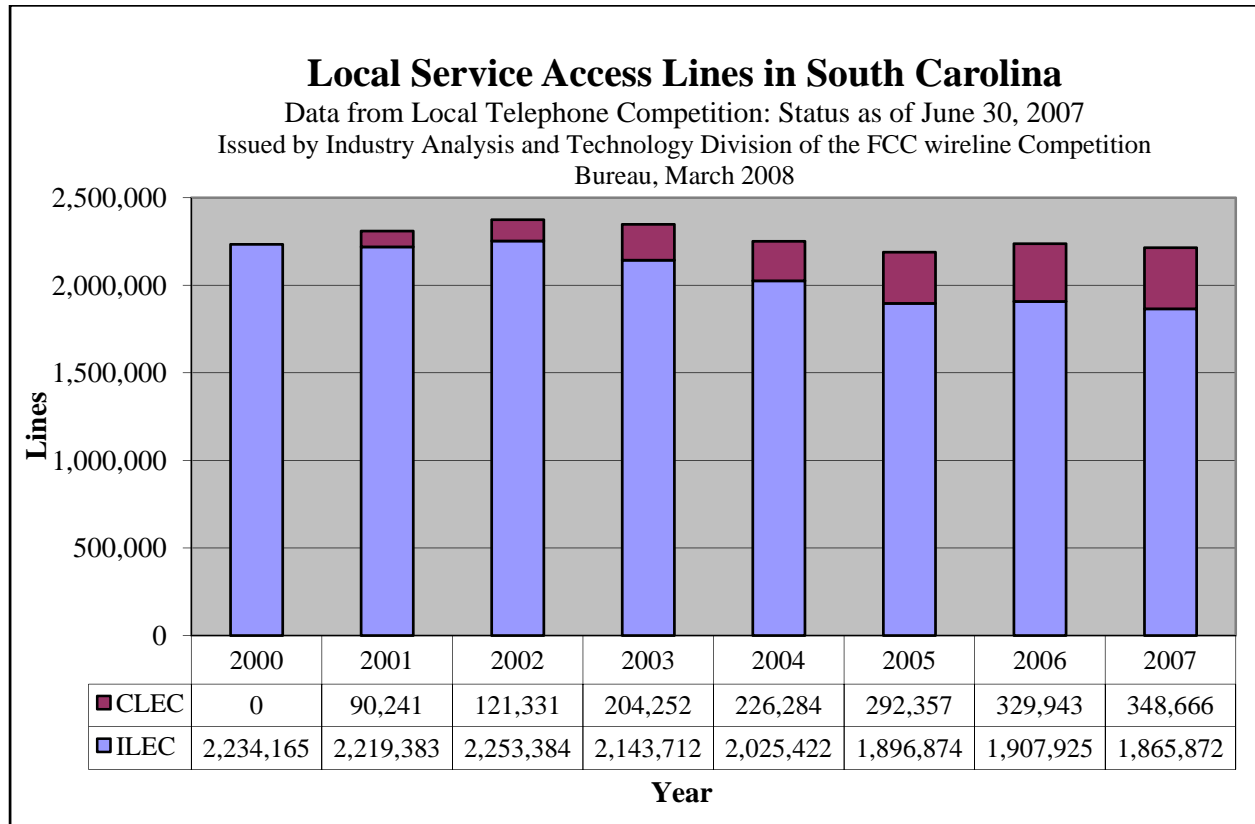
## **Local Exchange Telecommunications Market**

The Local Exchange Telecommunications Market is defined as the delivery of telephone service over a wired or physical line, and it is measured by the number of access lines or telephone lines in service. Local exchange services (or telephone services) are provided by Incumbent Local Exchange Carriers (ILECs) and Competitive Local Exchange Carriers (CLECs). ILECs are the traditional telephone companies that existed prior to the Federal Telecommunications Act of 1996. CLECs entered the market after the Telecommunications Act of 1996 was enacted by Congress, and opened the previously monopoly controlled local telephone market to entry by competing telecommunications vendors.

South Carolina wired access lines peaked in 2002 and then declined in 2003, 2004, and 2005. This trend may be attributed to the increasing number of households replacing their

wireline telephone with a wireless phone or a phone that delivers its service over the Internet (Voice over Internet Protocol or VoIP). More recently, Federal Communications Commission (FCC) data show a leveling off in this declining trend as the total access lines in South Carolina served by both ILECs and CLECs increased in 2006 and then decreased slightly in 2007.

**Chart 1: Local Service Access Lines**



Three concepts characterize what is occurring in the local telecommunications market: consolidation, convergence, and change. Consolidation is the result of mergers and acquisitions, (one company purchasing another or one company merging with another – to make a larger company) and means that consumers and businesses ultimately have fewer choices. As covered in last year's annual report, consolidation explains the merger of AT&T with BellSouth and the acquisition of MCI by Verizon. In 2007, CLEC lines grew by 5.7%, but the number of carriers declined by 15% (Table 1).

Convergence is a technological phenomenon. The technologies behind telephone service, cable TV, internet, and wireless are all converging; allowing the different services to be delivered on different or competing networks. For example, upgraded cable TV networks can now deliver internet and telephone service in addition to cable TV service, and as a result, cable TV companies continued to add telephone and internet customers. Additionally, telephone companies are expanding their high-speed access for both internet service and a new form of video service, and wireless companies are upgrading their networks to offer broadband (high-speed) internet services and even video.

The ORS considers change a critical component of the current telecommunications market, because consumers continue to change the way they purchase voice communications services. As one example, consumers appear to be increasingly opting for wireless or VoIP-based telephone service instead of the more traditional wireline telephone service. This may explain much of the decline in the number of access line in South Carolina.

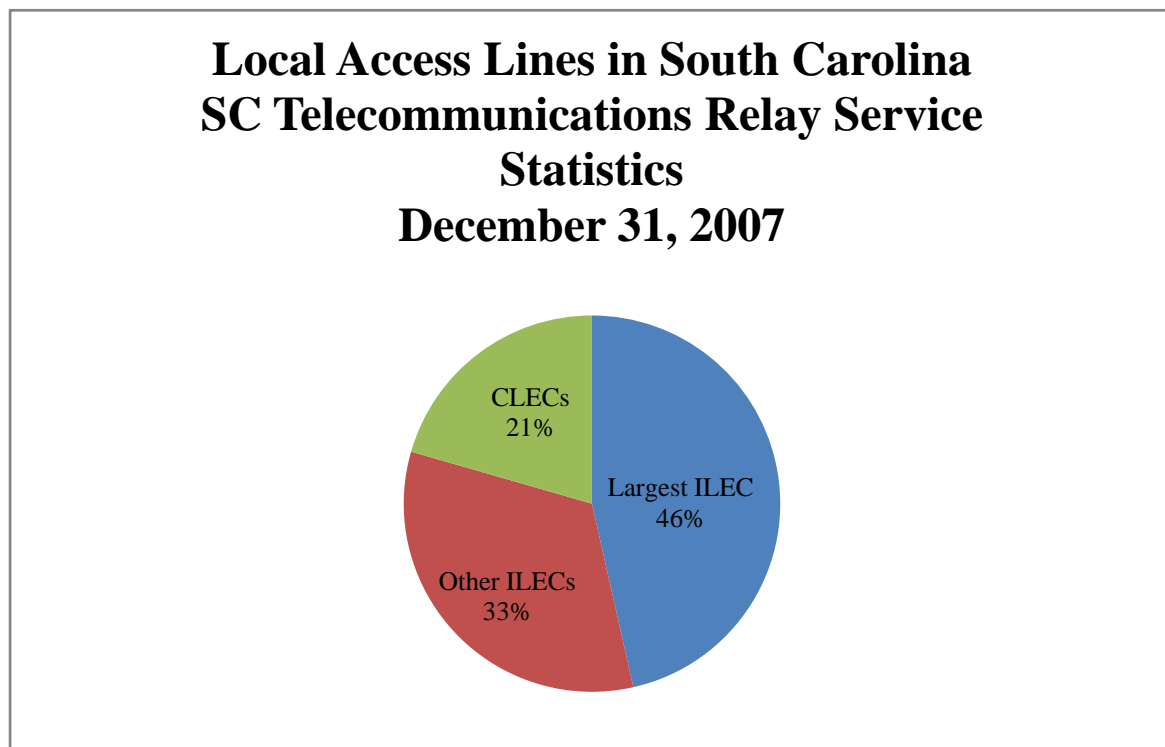
### **Incumbent Local Exchange Carriers**

During 2007 there was very little change among the ILECs in the state. Four of the state's ILECs applied for and were granted Alternative Regulatory status under Section 58-9-576 of the South Carolina Code of Laws. This means that 21 of the state's 25 ILECs are operating under the Alternative Regulation provisions of the Code.

### **Competitive Local Exchange Carriers**

CLEC market share grew again in 2007, increasing from 18% to 21% of the local exchange market. As mentioned above, access lines for these companies grew in 2007, increasing from 329,943 access lines in 2006 to 348,666 access lines.

**Chart 2: Local Access Market Share - Wireline Providers**



The state's largest ILEC lost 2% of its share declining from 48% in 2006 to 46% in 2007. The "other ILECs" also lost market share, dropping from 34% in 2006 to 33% in 2007. In this dynamic market it is difficult to pinpoint the source of these market changes, but an increasing number of residential customers are switching to the telephone service offered by their cable TV company (cable TV access lines are counted as CLEC lines in Table 2), while others are choosing wireless service as their only mode of voice communications. Chart 3 below, illustrates the growth in market share that South Carolina's CLECs have experienced since 2000.

**Chart 3: CLEC Market Share Growth**

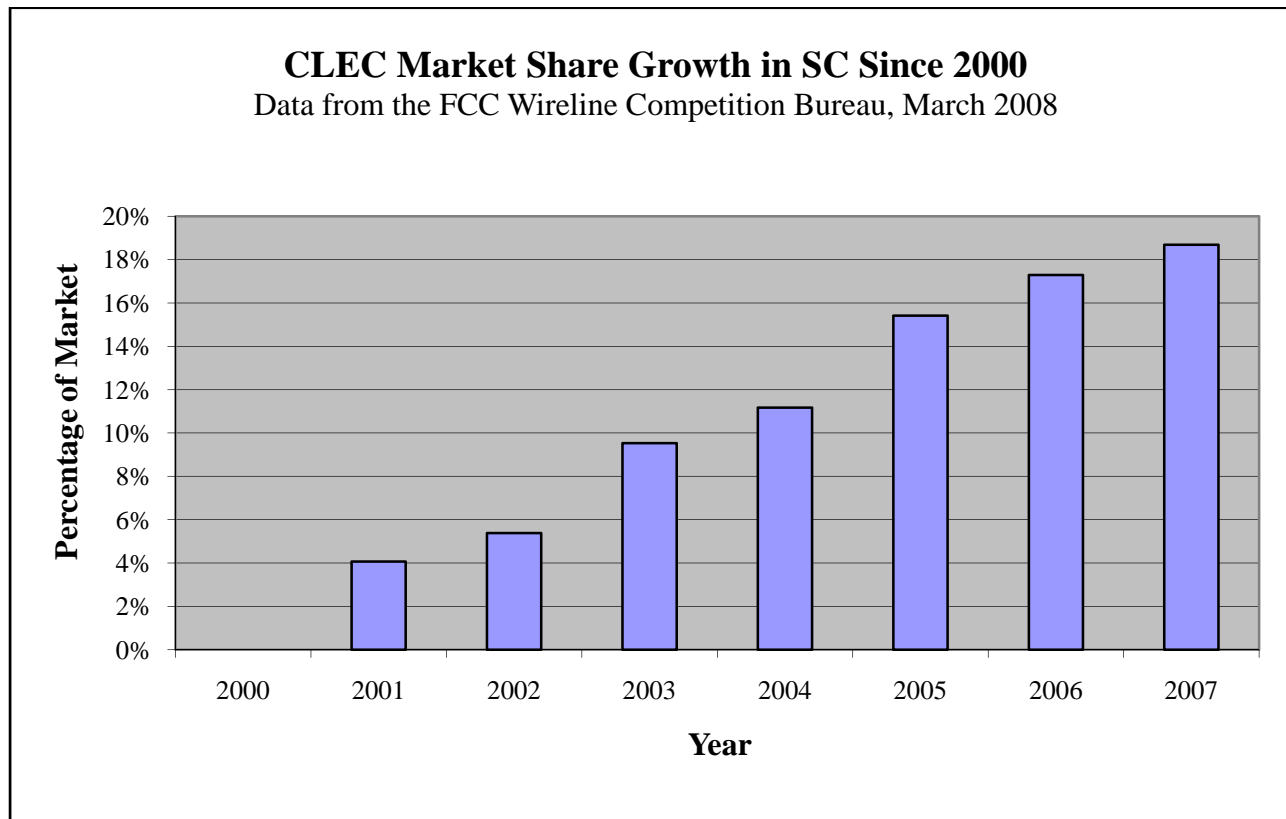


Table 1 takes a closer look at some of the change occurring among CLECs in the 2005 to 2007 timeframe. The number of CLECs with more than 20,000 access lines fell to five in 2007. This is a decrease from the six carriers who reported having more than 20,000 access lines last

year. At the same time CLECs with 10,001 – 20,000 access lines grew from two to five during the year 2007. For comparison, in 2006, the largest 8 CLECs held 71% of CLEC access lines, while in 2007 the largest 10 CLECs hold 77% of the lines. In essence 7% of the state's CLECs have captured nearly 80% of the lines served by all CLECs.

**Table 1: CLEC Access Lines**

<b>Number of Lines</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>% of 2007 CLEC Lines</b>
CLECs With No Lines	132	91	76	0%
CLECs with 1-1,000 Lines	38	39	28	1%
CLECs with 1,001-10,000 Lines	28	28	27	22%
CLECs with 10,001- 20,000 Lines	4	2	5	17%
CLECs with more than 20,000 Lines	4	6	5	60%
Total Number of CLECs in South Carolina	206	166	141	100%

During 2007, the trend of CLECs exiting the local market continued with the number of carriers declining from 166 to 141. While the total number of competitive carriers in South Carolina declined, CLECs continued to gain access lines and market share as mentioned above.

### **Alternative Regulation**

Prior to the introduction of competition in the telecommunications market, all incumbent local exchange carriers' prices were regulated based on a study of their rate of return and earnings. With the advent of a competitive telecommunications environment and the passage of the Telecommunication Act of 1996, the South Carolina General Assembly has passed various forms of regulation for the telecommunications industry. These legislative changes allowed



ILECs to be regulated in a more flexible manner if the company could show that competition exists for their services. Over the years, ILECs began to shift to alternative regulation based on the fact that they had interconnection agreements with competitive companies or based on a demonstration of the general availability of wireless services by two or more unaffiliated wireless carriers in their territory. This trend of South Carolina's ILECs moving to the more flexible alternative regulation continued in 2007. Of South Carolina's 25 ILECs, 22 have now elected and qualified for alternative regulation (there were 21 as of year-end 2007). Eleven of those companies cited interconnection agreements as justification for moving to alternative regulation, while the other eleven pointed to wireless service availability as their reason for alternative regulation.

Under this statutory plan, regulatory scrutiny concerning the pricing of services is relaxed. The statutes set out limitations with regard to the pricing of basic local exchange services and cap the amount of revenues which can be realized by increased pricing for services other than local exchange rates. ILECs qualifying for alternative regulation are also allowed to offer packages of bundled services on a non-regulated basis. This pricing flexibility gives carriers the ability to set the price of bundled services competitively with traditionally tariffed services, thus driving consumer demand in the most beneficial direction.

**Table 2: Alternative Regulation**

<b>Carrier</b>	<b>Alt. Reg. – Intercon- nection Effective Date</b>	<b>Alt. Reg. – Wireless Effective Date</b>	<b>Rate of Return Regulation</b>	<b>CLEC Affiliate</b>
United Telephone Company of Carolinas (Embarq- formerly Sprint)	29-Sep-97			Embarq Communications, Inc.
BellSouth Telecommunications	13-Aug-99			BellSouth Long Distance
Verizon South, Inc.	14-Oct-00			Verizon South
Windstream South Carolina	27-Sep-02			Windstream Communications
Horry Telephone Coop.	30-Jan-03			HTC Communications, Inc.
PBT Telecom	18-Feb-06			PBT Communications
Home Telephone Co.	7-Apr-06			Home Telecom, LLC
West Carolina Rural Tel. Coop.	16-Oct-06			West Carolina Communications
Piedmont Rural Telephone Coop.	12-Jan-07			PRT Communications, LLC
Lockhart Telephone Co.	9-Aug-07			Fairfield Communications
Farmers Telephone Coop.	1-May-08			FTC Diversified
Bluffton Telephone Co.		4-Mar-05		Hargray, Inc.
Hargray Telephone Co.		4-Mar-05		Hargray, Inc.
McClellanville Telephone Co. (TDS)		30-May-05		
Norway Telephone Co. (TDS)		30-May-05		
St. Stephen Telephone Co. (TDS)		30-May-05		
Williston Telephone Co. (TDS)		30-May-05		
Fort Mill Telephone Co. dba Comporium		1-Aug-05		PBT Communications dba Comporium
Lancaster Telephone Co. dba Comporium		1-Aug-05		PBT Communications dba Comporium
Rock Hill Telephone Co. dba Comporium		1-Aug-05		PBT Communications dba Comporium
Chester Telephone Co.		9-Aug-07		Fairfield Communications
Ridgeway Telephone Co.		9-Aug-07		Fairfield Communications
Chesnee Telephone Co.			<b>X</b>	
Palmetto Rural Telephone Coop.			<b>X</b>	Palmetto Telephone Communications
Sandhill Telephone Coop.			<b>X</b>	

### **Telecommunications Service Pricing**

Basic local exchange service rates charged by incumbent local exchange carriers have remained relatively stable in recent years. The major reason for this pricing stability is that when an ILEC chooses to move to alternative regulation as discussed above, a two-year moratorium is

placed on increases on basic service rates. However, some small ILECs - whose basic exchange rates were priced below the statewide average for residential and business rates - have elected to increase those rates to the statewide average rate. Upon pricing basic exchange rates at the statewide average rate, the small carriers are then subject to the statutory two-year moratorium on increases for basic exchange rates.

Only one of the larger local carriers increased their local exchange rates during the review period. The bulk of changes to ILEC rates were predominately increases in what is described by the statute as Other Services, which are all services other than basic exchange services. From a retail perspective, these services are generally characterized as discretionary, vertical, or non-basic services such as caller identification, three-way calling, and other custom-calling features. Other Services also includes wholesale services which are services required by other carriers to provision local- and long-distance services. A small percentage of the local carrier price changes related to rates for directory assistance and calling plans. Most new tariff activity came from additional service offerings by the ILECs. Data-related offerings such as frame relay and high bandwidth were dominant. Tariff changes were substantial in the CLEC arena. However, applications for entry into the South Carolina market to provide competitive local exchange service tapered off during 2007. As with the ILECs, CLECs introduced new service offerings that should provide more choices to consumers. In addition, rate increases were requested that affected Calling Plans, Vertical Features, Presubscribed Operator Services, and Directory Assistance. Very few changes occurred in the area of Switched Access Service.

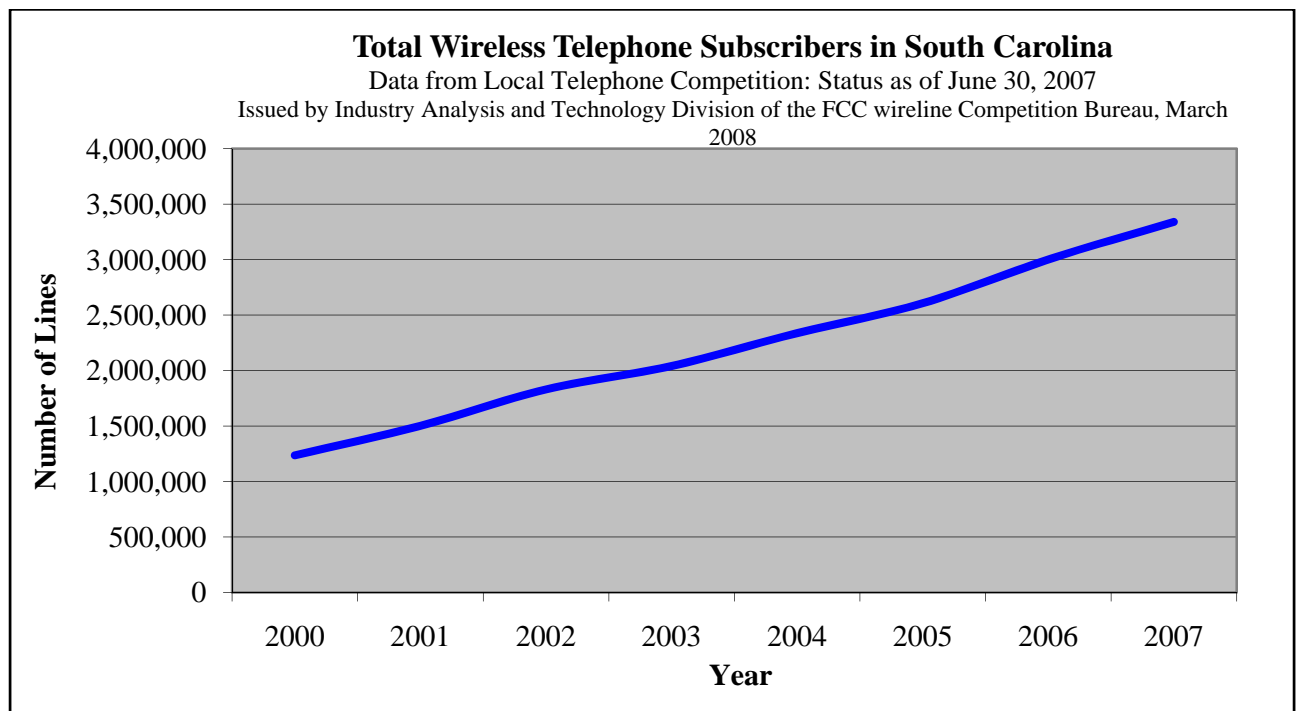
Interexchange Carriers (IXCs), commonly referred to as Long Distance Providers, filed a large number of tariff revisions. Like other carriers, the majority of tariff changes were for new service offerings instead of rate changes for existing services. Some of the IXCs which have

local affiliates have introduced unlimited calling options that are priced similarly to plans introduced into the market by competitive carriers. Where rate changes were requested, they were predominately increases for both business and residential consumers.

### **Wireless Carriers**

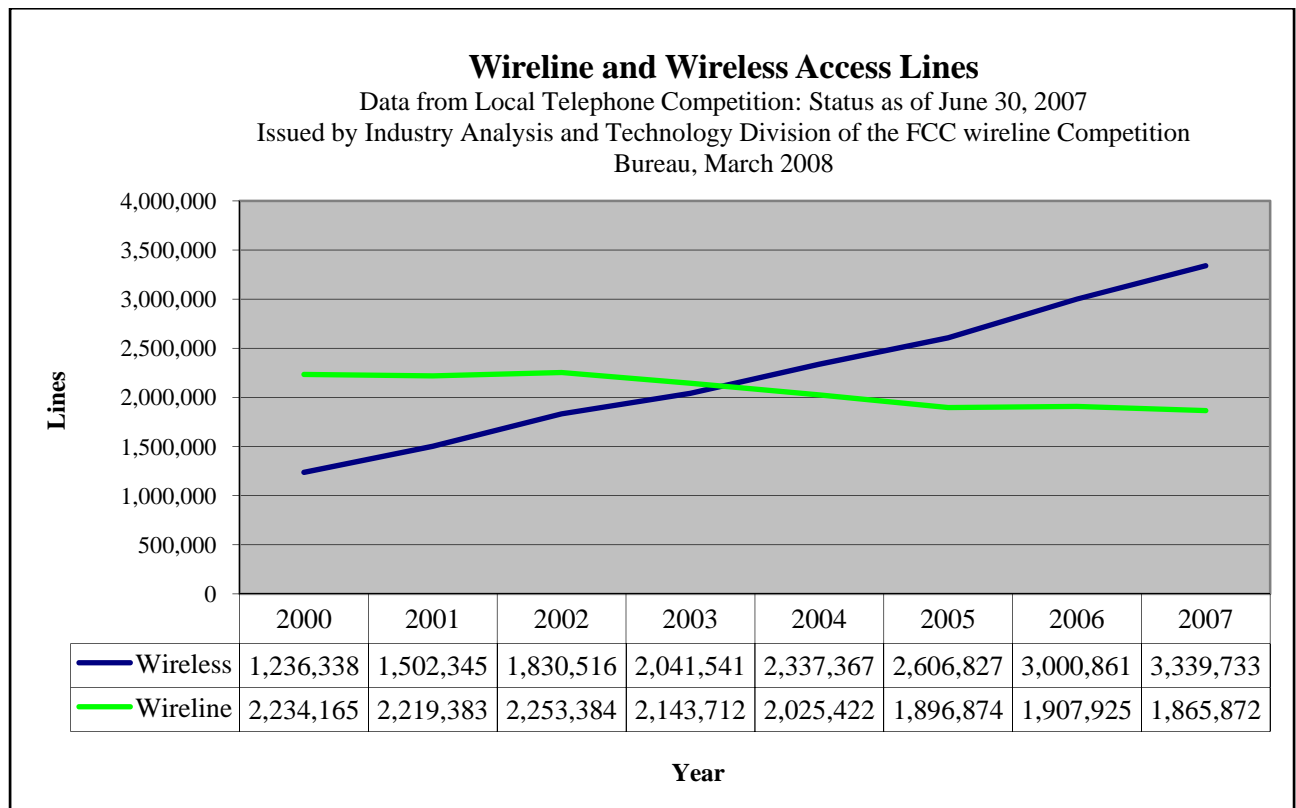
Throughout the country, wireless access lines continue to grow. In 2007, thirteen wireless carriers operated in South Carolina, up from twelve in 2006. These 13 wireless companies reported 3,339,733 wireless subscribers in South Carolina, an increase of over 11% from the previous year. Wireless service has seen tremendous growth nationwide and South Carolina is no exception. In 2007 wireless penetration exceeded 75% of the population; in other words, of the state's 4.4 million residents, 3.3 million carried a cell phone. Chart 4 shows the steady growth in wireless lines in South Carolina from 2000 to 2007.

**Chart 4: Wireless Subscribers in SC**



While wireless usage is trending upward, wireline usage is declining or flat. These results indicate an evolution or change in the way consumers purchase telecommunications service. Increasingly, individuals are choosing to purchase personal, mobile communications services rather than household or family based wireline service. Chart 5 tracks a comparison of total wireless and wireline access lines in the state from 2000 to 2007.

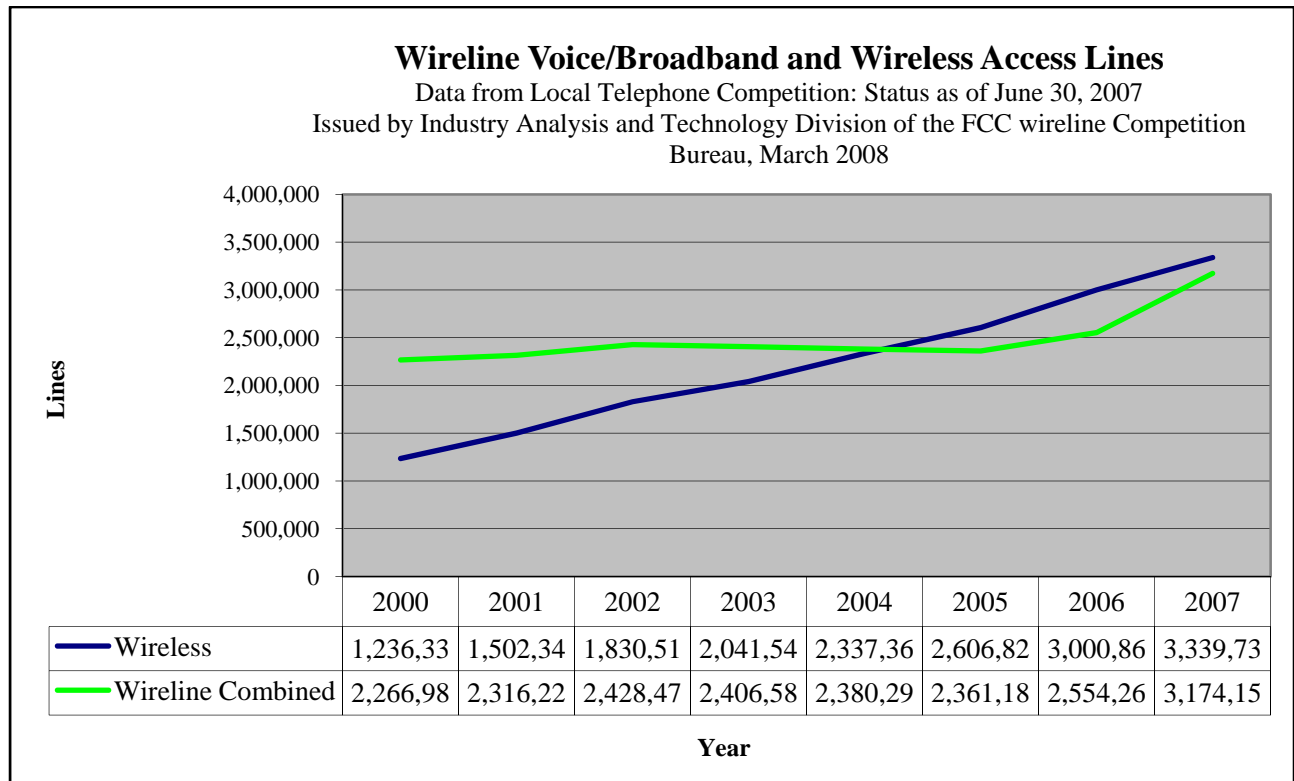
**Chart 5: Wireline and Wireless**



While Chart 5 may suggest wireline carriers are facing declining revenues in comparison to the continued growth of their wireless competitors, market activity indicates that wireline carriers are coupling their traditional voice service with broadband internet service to create additional revenue streams and remain competitive in the market. Chart 6 shows the combination of wireline voice with broadband in comparison to wireless lines. When looking at the data in this manner, the growth of both markets is more comparable. The efficiency of

providing broadband and voice traffic over a single line should provide additional stability to the wireline markets. Wireless providers are also looking to continue their deployment of wireless broadband.

**Chart 6: Broadband and Wireless**



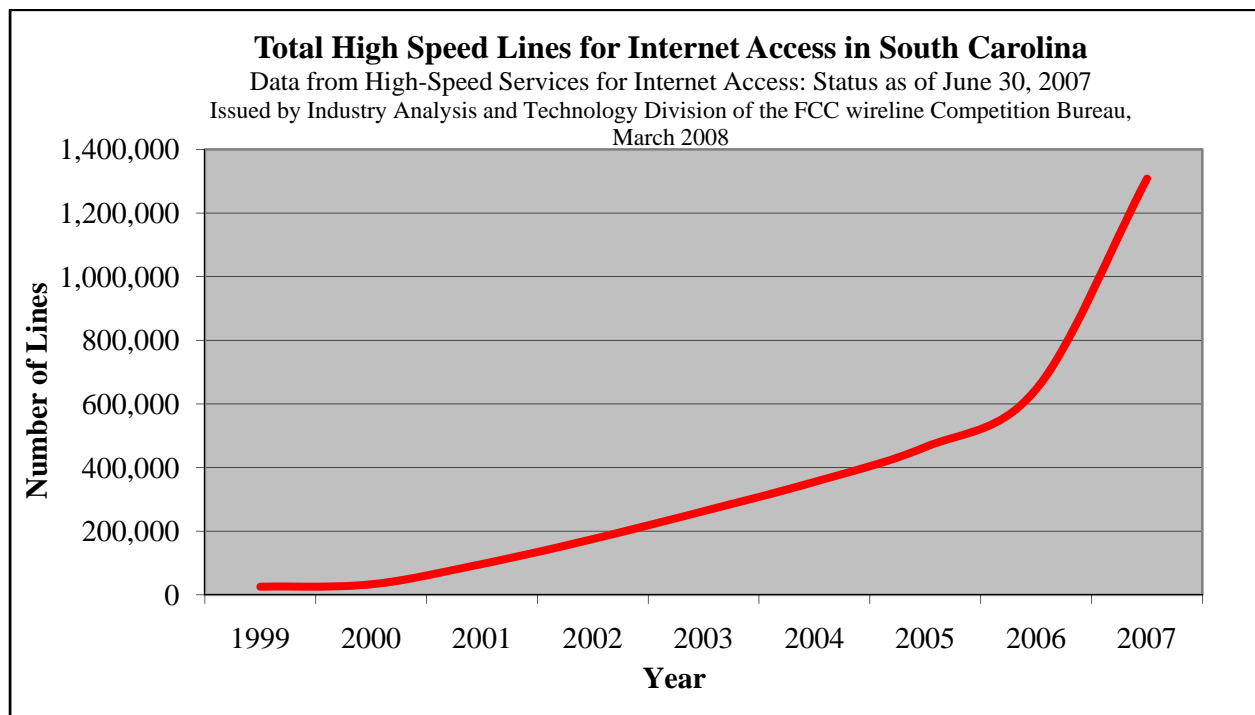
### **Broadband Deployment**

Underlying the industrial, technological, and residential growth occurring in South Carolina is the development of enhanced broadband technologies and their deployment throughout the state. As an enabling technology, broadband deployment plays an important role in the economic growth of South Carolina.

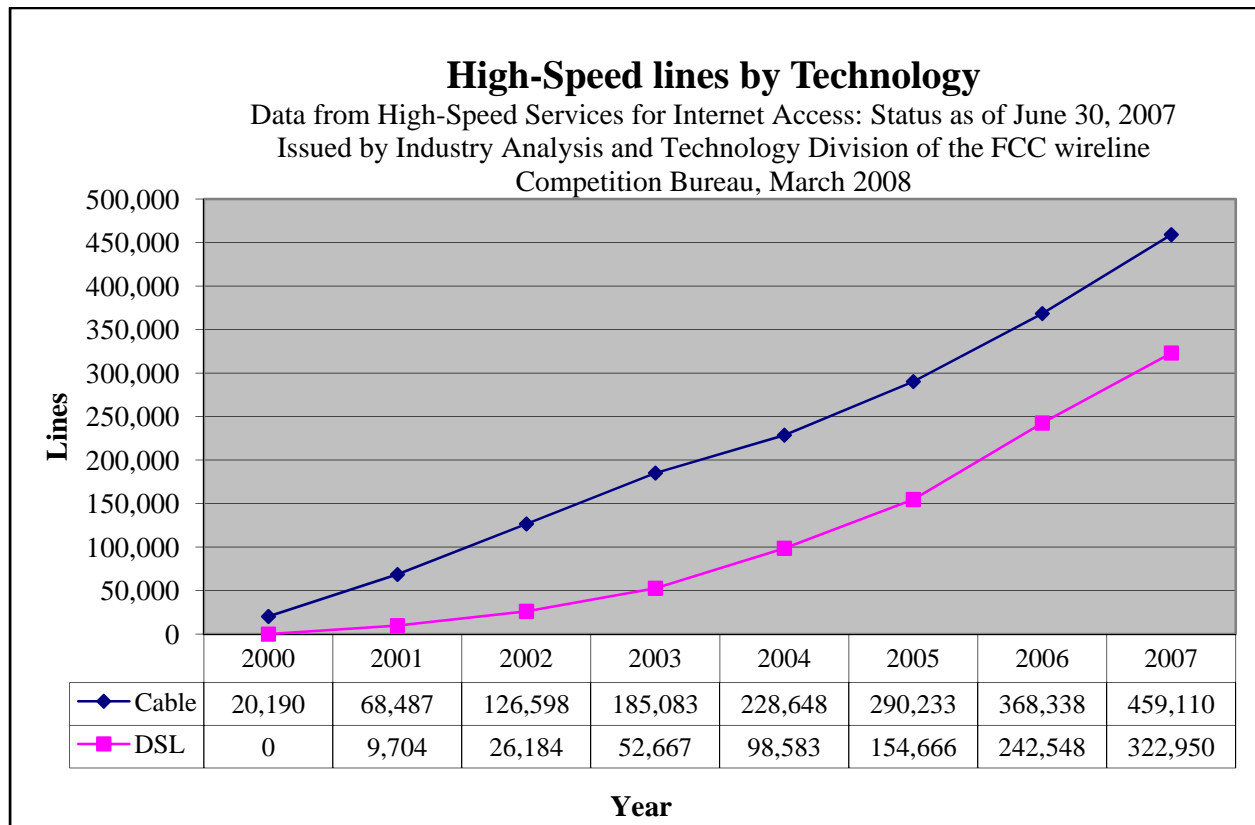
From 1999 to 2006 broadband access grew at a steady rate in South Carolina, rising from 25,229 in 1999 to 645,886 in 2006 as demonstrated in Chart 7. In 2007, however, the state's

high-speed lines more than doubled, growing by over 102%, jumping dramatically to 1.3 million. Total U.S. growth, while significant, was roughly half that of South Carolina, growing at a rate of nearly 54%. Quoting from the last Annual Competition Report, released in November 2007, “If this growth continues at the current rate, South Carolina will have over 1 million high-speed access lines in service by 2011.” The substantial increase in the growth rate has allowed the state to exceed the 1 million high-speed access line mark much more quickly than expected.

**Chart 7: Internet Access**



Prior to 2006 broadband access was delivered primarily using two technologies: cable modem (using mostly copper-coax lines offered by cable companies) and Digital Subscriber Line service (DSL) (using copper-pair offered by local exchange carriers). Based on 2007 data, the market share related to these technologies is 459,110 lines for cable modem and 322,858 lines for DSL. Chart 8 shows the growth of high-speed lines by both technologies from 2000 to 2007.

**Chart 8: High-Speed Technology**

In 2006, the FCC reported high-speed access lines attributable to wireless and satellite carriers to be 23,581. In the 2007 Annual Competition Report, the ORS indicated that wireless carriers are beginning to provide a wireless option for high-speed internet access services. In a recent presentation by CTIA, a national wireless carrier association, the presenter indicated that, according to FCC data for the period from December 2005 to June 2006, 59% of new high-speed lines were obtained from Commercial Mobile Radio Service (wireless) providers. Today, wireless operators are aggressively entering the broadband market through enhancement to the wireless network.



In reviewing the FCC's 2007 High-Speed Services report<sup>1</sup>, the ORS determined that the FCC was reporting high-speed access lines attributable to wireless and satellite carriers to be 506,010. This is a 20-fold increase in these high-speed access lines, and accounts for nearly all of the difference between the totals on Chart 7 and Chart 8. The ORS will be watching carefully to see how high-speed access lines continue to develop over the next few years.

### **Consumer Services**

In 2007, as in previous years, consumers complained most about service quality, billing issues, and non-regulated issues. The ORS tracking of consumer complaints during 2007 covered a wide range of issues for both regulated and non-regulated local telephone services.

---

<sup>1</sup> High-Speed Services for Internet Access: Status as of June 30, 2007, Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, March 2008.

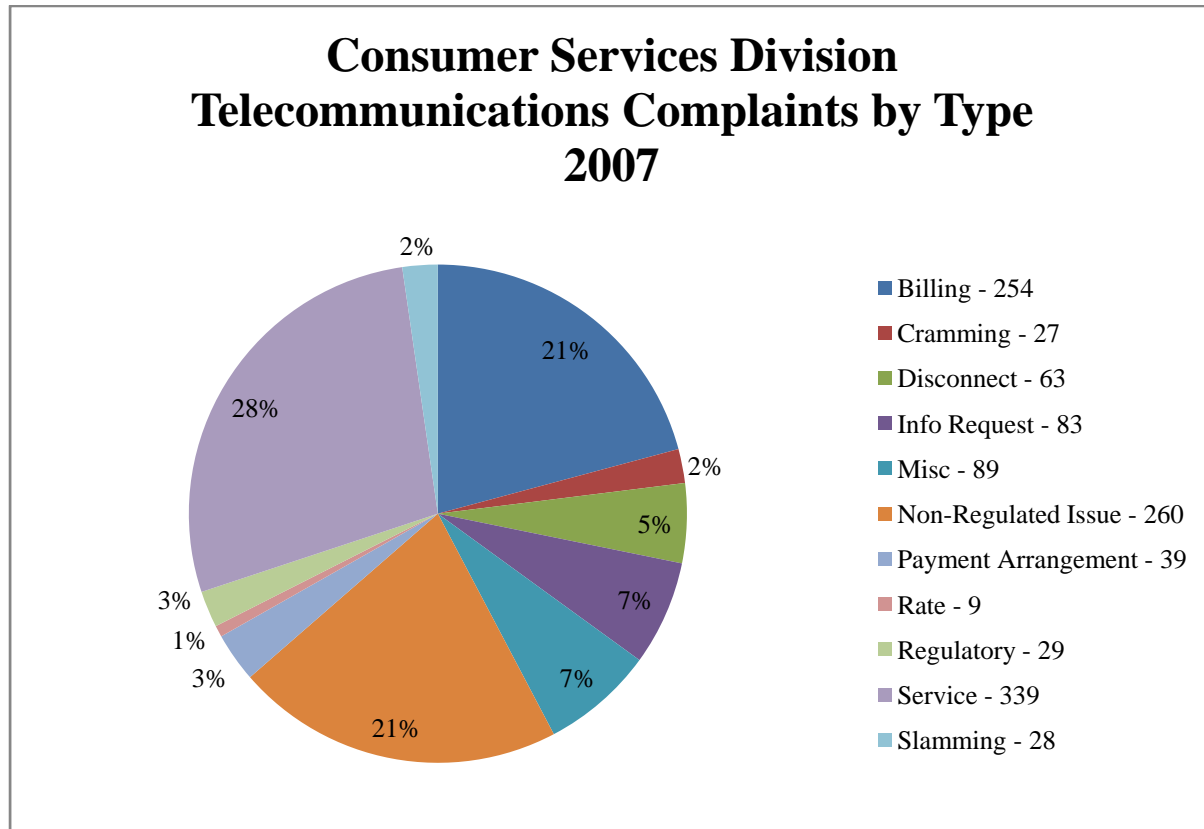
**Chart 9: Consumer Complaints**

Chart 9 depicts a categorical breakdown of complaint calls received by the ORS during 2007. Service quality continues to be the largest area of complaints with 28% of the total falling in that category.

### **The Regulatory Landscape**

#### **Intercarrier Compensation**

In the 2007 Annual Report, the ORS provided a summary of the FCC's attempts to resolve intercarrier compensation issues. The FCC has yet to adopt any of the many proposals before it.

### **Designation of Eligible Telecommunications Carriers (ETCs)**

Eligible Telecommunications Carriers are companies designated by the states and, in some cases, by the FCC to be eligible to receive support from the federal Universal Service Fund. Federal law and FCC rules allow both ILECs and CLECs to be designated as ETCs. In 2007, three wireless companies applied for and were approved as competitive ETCs (CETC) in South Carolina. These companies are capable of drawing additional federal funds into the state for use in building out wireless networks in underserved areas of the state.

South Carolina is one of seven states which did not receive federal USF funds for CETCs in 2006. In 2007, CETCs across the nation received over \$1 billion in high-cost support from the federal USF, with North Carolina receiving approximately \$11 million and Georgia benefiting by over \$7 million. In early 2007, the Federal-State Joint Board on Universal Service Fund recommended to the FCC that an interim cap be placed on the distribution of federal USF monies as a measure to curb the growth of the federal USF. Based on the FCC's recent order, a cap is now in place that limits South Carolina's ability to draw from the fund.

### **Conclusion**

Based on data the ORS has gathered while investigating the status of local telecommunications competition in South Carolina over the past two reports, the wireless market is growing steadily while the landline market is declining somewhat, due at least in part to wireless substitution. Meanwhile, although the number of CLEC competitors declined in 2007, the remaining CLECs are growing in market share and providing a healthy level of competition.

The major competition for traditional voice telephony in the residential sector continues to come from digital phone, VoIP and wireless technologies. The convergence of technology platforms is enhancing consumer choice, and driving consumer demand for “triple play” type services.