

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Business Data Services in an Internet Protocol Environment)	WC Docket No. 16-143
)	
Special Access Rates for Price Cap Local Exchange Carriers)	WC Docket No. 05-25
)	
AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services)	RM-10593
)	

COMMENTS OF AT&T INC.

James P. Young
Christopher T. Shenk
Jacqueline G. Cooper
Kyle J. Fiet
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000

Keith Krom
Gary L. Phillips
David L. Lawson
AT&T Inc.
1120 20th Street, N.W.
Washington, D.C. 20036
(202) 457-3058

Attorneys for AT&T Inc.

June 28, 2016

TABLE OF CONTENTS

INTRODUCTION AND SUMMARY1

I. THE MARKETPLACE FOR BDS IS ROBUSTLY COMPETITIVE AT ALL LEVELS, AND INCREASED REGULATION OF BDS WOULD BE COUNTERPRODUCTIVE.10

A. The Near-Ubiquity of Facilities-Based Alternatives Establishes Beyond Reasonable Dispute That BDS Is Highly Competitive For All Bandwidths.....11

B. The Commission Cannot Rely on the Rysman Paper as Evidence Of Market Power For DS1 and DS3 Services.17

1. The Rysman Regression Analyses Are Not Reliable.18

2. The Effects Rysman Shows Are Too Small to Justify New Regulation....22

C. The Commission’s Remaining “Indicia” of Market Power Are Makeweights.24

II. THERE IS NO BASIS FOR REGULATION OF ETHERNET SERVICES.....28

III. ANY NEW COMPETITIVE MARKET TEST MUST ACCOUNT FOR ALL SOURCES OF COMPETITION, BE SIMPLE TO ADMINISTER, AND SUPPORTED BY DATA.36

A. The Competitive Market Test Proposed In The IRW White Paper Accurately Identifies Census Tracts Where Most Buildings and Demand Can Be Served By Multiple Providers Of BDS.37

B. The Commission Should Not Adopt The Product Market Definition For BDS Proposed In The *Notice*, Nor Should The Commission Evaluate Competition Based On Customer Classes.41

1. The BDS Product Market.....42

2. Customer Classes.....47

C. Number of Competitors50

IV. THE COMMISSION SHOULD NOT MODIFY THE X-FACTOR OR ADJUST THE CURRENT PRICE CAPS FOR LEGACY TDM BDS.....52

A. There Is No Justification for a New BDS-Specific X-Factor.53

B. The Commission’s Proposals For A New X-Factor To Be Applied Prospectively Have Significant Deficiencies.....56

C. The Commission’s Proposed “Baseline Price Cap Level Adjustment” Would Also Be Unlawful.....62

REDACTED – FOR PUBLIC INSPECTION

V.	THE COMMISSION SHOULD REJECT ITS ADDITIONAL PROPOSALS FOR REGULATION OF “NON-COMPETITIVE” SERVICES.....	64
A.	The CLEC Proposal To Add An Additional New Layer of Regulation For “Wholesale” Purchases Is Unnecessary And Would Impede Investment And Slow The Transition To IP-Based Services.	65
B.	The Commission Should Not Issue Blanket Regulations Governing Terms And Conditions In Commercial Agreements And Tariffs.....	71
1.	The Alleged Tying Provisions In Commercial Contracts.....	72
2.	The Commission Should Not Regulate Percentage Commitments, Term Commitments, Upper Percentage Thresholds, Or Overage Charges.....	77
C.	The Commission’s Proposal to “Detariff” TDM Services In Name Only Would be Unlawful.	80
VI.	THE COMMISSION’S PROPOSALS FOR REGULATION IN “COMPETITIVE” AREAS WOULD BE UNLAWFUL AND UNSUPPORTED.....	81
A.	Non-Disclosure Arrangements.....	81
B.	The Commission Should Not Extend The Prohibitions Adopted In The Tariff Investigation Proceedings To Other Agreements And Tariffs.	83
	CONCLUSION.....	85

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Business Data Services in an Internet Protocol Environment)	WC Docket No. 16-143
)	
Special Access Rates for Price Cap Local Exchange Carriers)	WC Docket No. 05-25
)	
AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services)	RM-10593
)	

COMMENTS OF AT&T INC.

AT&T respectfully submits these comments in response to the Further Notice of Proposed Rulemaking released on May 2, 2016 in the above-captioned matter.¹

INTRODUCTION AND SUMMARY

In many respects, the *Notice* is an enigma. The Commission, and indeed the Obama Administration, have consistently emphasized that it is a national priority to facilitate and hasten the IP transition. Yet, even as customers are abandoning legacy services in favor of IP services at a remarkable clip, the *Notice* proposes to ratchet down the prices of legacy services, which can only slow that process. These proposals are all the more head-scratching because the record here

¹ Tariff Investigation Order and Further Notice of Proposed Rulemaking, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (rel. May 2, 2016) (“*Notice*”).

– indeed, the *Notice* itself – is replete with facts demonstrating that the BDS market is robustly competitive at all levels. The only conclusion one can draw is that the Commission started down this path of reregulation under the misimpression that the market was less competitive than it actually is, and now that the record has disproved its theory, it is moving forward anyway.

But the Commission has insisted from the beginning that any decision in this proceeding would be fact-based, and the Commission must follow the facts where they lead. The Commission’s data collection reveals that, as of 2013, virtually all buildings with special access demand were either connected to, or within one half mile of, competitive fiber, even without taking into account cable HFC facilities. Since the *Notice* recognizes that “fiber-based competitive supply within at least half a mile generally has a material effect on prices of BDS,”² it necessarily follows that existing competitive facilities are materially constraining prices virtually everywhere there is special access demand. In fact, 85% of the bandwidth AT&T sells is within *1000 feet of two competitive networks*. Thus, even when measured by a stricter gauge, competition for BDS services is robust and ubiquitous. Nor is this competition confined to high capacity services: as of 2013, 82% of AT&T’s sub-50 Mbps bandwidth was within 1,000 feet of competitive fiber.³

Market share data reported in the *Notice* tell a similar story. According to the *Notice*, even as of 2013, competitors accounted for a majority of BDS revenue – again, without taking

² *Notice* ¶ 161.

³ Second Supplemental Declaration of Mark Israel, Daniel Rubinfeld and Glenn Woroch, *Special Access for Price Cap Local Exchange Carriers*, Docket No. 05-25, RM-10593, at 10 (filed April 20, 2016) (“IRW Second Supp. Decl.”), attached to Letter from Christopher T. Shenk (AT&T counsel) to Marlene H. Dortch (FCC), WC Docket No 05-25; RM-10593 (April 20, 2016).

cable into account.⁴ And there is every reason to believe that competitors today account for an even larger (and growing) majority of BDS revenues.

Based almost entirely on a study performed at the Commission’s behest by Professor Marc Rysman,⁵ however, the *Notice* claims that incumbent LECs continue to exercise market power in BDS pricing. For example, the Rysman study presents the results of regression analyses purporting to show that price cap LECs charge 3.2% less for DS1 services in census tracts where another provider can serve a customer in the same census tract.⁶ But even Professor Rysman admits his regressions are “problematic” and must therefore be interpreted with extreme caution,⁷ and for good reason. As Drs. Israel, Rubinfeld, and Woroch explain, it is impossible to tell whether the lower prices he found are caused by competitive entry, or whether they merely reflect, in whole or in part, the favorable economic conditions, such as lower costs and/or higher revenue opportunities that may attract competitive entry in the first place. Although Professor Rysman acknowledges and tries to address this problem, the problem is not actually fixable because, as Drs. Israel, Rubinfeld, and Woroch explain, it is inherent in the limitations of the data. Because correlation is not the same thing as causation, the Rysman analysis does not present reliable evidence of market power in the pricing of BDS.

In all events, even if the 3.2% price differential described in the study actually were attributable in its entirety to the presence or absence of competitive entry, such a small differential does not establish a foundation for an overhaul of BDS regulation. Professor Rysman himself acknowledges that this difference is “not especially large by the standards of

⁴ *Notice* ¶ 217, Figure 9.

⁵ Dr. Marc Rysman, *Empirics of Business Data Services*, White Paper, at 228-29 (April 2016) (attached as Appendix B of *Notice*) (“Rysman White Paper”).

⁶ *Id.* at 228.

⁷ *Id.*

competition analysis,”⁸ and that is an understatement: such a small differential would not even register under the Justice Department’s SSNIP test.⁹

While there is thus no reliable data in the record warranting regulatory changes for legacy TDM services, there is even *less* basis for reregulating Ethernet services. Professor Rysman found *no* evidence of market power in his regressions for Ethernet and other BDS with speeds of 45 Mbps and higher.¹⁰ And, although Professor Rysman did not test whether market power existed for Ethernet services below 45 Mbps, Drs. Israel, Rubinfeld, and Woroch *did* (using the same method Professor Rysman used in his other regressions) – and they found no evidence of market power for those services either.¹¹

That should come as no surprise. Ethernet services have only gained popularity within the past decade, and no provider had (or has) an incumbent advantage for Ethernet services. A wide variety of ILECs, CLECs, cable companies, and others, have invested billions of dollars to deploy Ethernet services, and none has a port share in excess of twenty percent. There are nine

⁸ *Id.* at 228-29.

⁹ That test, contained in the US Merger Guidelines, is used by the Justice Department as a tool for defining markets. It looks at the effects of a small but significant non-transitory increase in price. Horizontal Merger Guidelines, U.S. Department of Justice and the Federal Trade Commission, § 4.1.2 (Issued Aug. 19, 2010), <https://www.justice.gov/atr/horizontal-merger-guidelines-08192010>.

¹⁰ Rysman White Paper at 229 (“[t]he effect for high-bandwidth lines is statistically insignificantly different from zero for census tract fixed effects and is positive for fixed effects”); *id.* at 226, n.31 (“[d]ue to timing constraints, the data set analyzed did not include packet-based services with bandwidths of 45 Mbps and less”).

¹¹ Mark Israel, Daniel Rubinfeld and Glenn Woroch, Analysis of the Regressions and Other Data Relied Upon in the Business Data Services FNPRM And a Proposed Competitive Market Test, *Business Data Services in an Internet Protocol Environment; Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 16-143, 05-25, RM-10593, at 26 (filed Jun. 28, 2016) (“IRW Second White Paper”). For this reason, Verizon and Incompas’ recent suggestion that the Commission should consider *all* sub-50 Mbps services to be “non-competitive” would be patently absurd, because the record (including the regression tools created by the Commission’s own expert) unequivocally refutes their claim.

Ethernet providers with port shares of four percent or more, and those nine providers include four CLECs and three of the nation’s largest cable companies.¹² Level 3, a CLEC, is the second largest Ethernet provider.¹³ And other providers – *i.e.*, those with port shares under 4 percent – together have, in the aggregate, port share in excess of 20 percent.¹⁴

Thus, far from providing a basis for rescinding regulatory forbearance for Ethernet services, the record demonstrates that Ethernet services are provided in a robustly competitive environment with no evidence of pricing above competitive levels. Given that evidence, the Commission should continue its policy of regulatory forbearance for these services, particularly since rescinding that policy will discourage broadband investment in contravention of longstanding Commission goals. Rescinding that policy would also surely fail judicial review. As the Supreme Court has explained, when an agency adopts “new policy” which “rests upon factual findings that contradict those which underlay its prior policy,” it must “provide a more detailed justification than what would suffice for a new policy created on a blank slate.”¹⁵ Here, the Commission would be unable to provide any fact-based justification, let alone the more detailed justification required under the law.

For all of these reasons (as described in more detail below), the record evidence provides no basis to re-regulate BDS, and it most certainly provides no basis for mandated price reductions. And it is that evidence, not preconceived assumptions that are belied by the facts or

¹² Vertical Systems Group, “2015 U.S. Carrier Ethernet LEADERBOARD” (Feb. 25, 2016), <http://www.verticalsystems.com/vsglb/2015-u-s-carrier-ethernet-leaderboard/> (“Ethernet LEADERBOARD”). *See also* Notice ¶ 83.

¹³ *See* Ethernet LEADERBOARD; Notice ¶ 83.

¹⁴ *See* Ethernet LEADERBOARD.

¹⁵ *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009); *see also id.* (“a reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy”).

pretend “compromises” between a CLEC and a sometimes ILEC¹⁶ – both of them net purchasers of BDS – that must control the decision in this docket. Therefore, the most sensible path forward is simply to terminate this proceeding. Although a more geographically granular Competitive Market Test for DS1 and DS3 services is not, as a matter of principle, objectionable, there is no evidence that the existing test is resulting in any appreciable harm, and replacing that test with another, more granular test will necessitate expensive modifications to billing systems that have been built to reflect MSA-based regulatory distinctions, while increasing transaction costs in contracting with customers. There is no good reason to impose those costs on the industry.

Nonetheless, if the Commission proceeds with a new, more granular Competitive Market Test, it must ensure that test is administratively feasible. The *Notice* seeks comment on a multi-layered, multi-factored set of parameters that might be incorporated in a replacement test, but those variables are both unnecessary and wholly impractical. A better approach that more properly balances the twin goals of more granularity and administrative feasibility would be to gauge competition for DS1 and DS3 services on a census-tract basis in accordance with the following simple and economically sensible test: DS1 and DS3 services are competitively provided in a census tract if two or more providers have deployed facilities in or within 2,000 feet of that census tract.

The 2013 data collected by the Commission confirms that this test is a highly accurate predictor of competition. According to the 2013 data, more than 90 percent of all ILEC buildings with BDS demand in these census tracts are within 2,000 feet of two or more providers, and these buildings account for more than 90% of BDS bandwidth in those census

¹⁶ Having shed substantial portions of its wireline operations, and with a pending purchase of XO Communications, Verizon, like Sprint, has become a net purchaser of BDS. Its joint proposal with Incompas is thus not a compromise, which requires two parties with divergent interests. It is simply joint advocacy to advance their common interests.

tracts. That is true regardless of whether the analysis is of all BDS services or only sub-50 Mbps services. Moreover, these 2013 metrics understate the true extent of competition *today* because they do not reflect the substantial competitive facilities-based expansions that have occurred since then. Accordingly, census tracts meeting this test can reliably be deemed “competitive,” and the Commission can and should eliminate price cap regulation for legacy TDM services in such areas.

The question then becomes what regulation should apply to legacy TDM services in areas the Competitive Market Test deems “non-competitive.” The Commission properly proposes to detariff such services and grant blanket contracting relief throughout all such areas, but the proposal to adopt a new, productivity-based, BDS-specific X-Factor should be rejected. Demand for DSn services is rapidly declining and carriers are in the process of retiring their legacy TDM facilities. Thus, there can be no reasonable expectation that price cap LECs will be able to achieve meaningful productivity gains in providing these services in the future. To the contrary, an increased X-Factor (and a one-time adjustment to these rates) intended to drive down the rates for legacy TDM services would dramatically slow the IP transition by giving customers an artificial incentive to remain on these legacy networks, which in turn will reduce incentives to invest in new broadband networks. In all events, to the extent a BDS-specific productivity offset could reasonably be calculated, it would be quite small. If the Commission intends to rely on broad, publicly available data sources, the only valid source would be the U.S. Bureau of Labor Statistics’ (“BLS”) official productivity data for the communications industry, which indicates that the X-Factor should be no more than 1.95 percent.¹⁷ An X-Factor of that magnitude is not

¹⁷ See Notice ¶ 407, Table 7; Mark E. Meitzen & Philip E. Schoech, Assessment of the FCC’s Proposed Options for the Special Access Price Cap X-Factor, Business Data Services in an Internet Protocol Environment; Special Access Rates for Price Cap Local Exchange Carriers;

likely to be sufficiently different from inflation over the waning lifetime of these services to warrant a rule change.

Nor is there any basis for a one-time adjustment to the price caps to account for productivity gains since 2005. Again, according to the Commission’s own calculations, the BLS data – which is the only one of the Commission’s proposed methodologies that actually attempts to measure productivity – indicate that the X-Factor over the 2005-2013 period was almost exactly the same as the inflation factor and thus would not support any reduction in the cap. Similarly, Professor Rysman’s regressions, to the extent reliable, find that the price cap LECs’ DS1 rates in competitive areas are only about three percent below the rates in “non-competitive” areas. Thus, Professor Rysman’s analysis confirms that price cap LECs could not possibly have achieved productivity gains since 2005 that would justify a large one-time adjustment to the caps applicable in non-competitive areas.

The Commission should also reject calls for new rules to govern how BDS is priced at wholesale. Any attempt to mandate wholesale discounts for BDS would violate Sections 201 and 202 as an improper (and long-prohibited) “use restriction.” The prohibition on use restrictions helped fuel the phenomenal growth of long-distance competition in the 1980s and 1990s, and there is no basis for suddenly abandoning that longstanding policy in favor of a mandated wholesale discount for BDS services. To the contrary, the Commission’s own data show that non-ILEC competitors have won *more than half* of all revenue for BDS,¹⁸ which belies claims that there is a systemic problem that requires reversal of longstanding precedent.

AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, WC Docket Nos. 16-143, 05-25, RM-10593, at 7-9 (filed Jun. 28, 2016) (“Christensen Paper”).

¹⁸ Notice ¶ 217, Figure 9.

CLEC arguments to the contrary are built entirely on isolated anecdotes, which AT&T and others have previously shown to be false. The Commission and antitrust courts alike have been extremely skeptical of the sort of “price squeeze” arguments the CLECs press here,¹⁹ and such arguments are especially implausible in the context of services like Ethernet, which are subject to robust competition. Firms like AT&T, which have only a small market share, would have no hope of effecting a price squeeze to drive out competitors.²⁰

In addition, suggestions that reregulation of BDS is necessary to facilitate wireless carriers’ transition to 5G are nonsense. To date, Sprint is the only wireless provider seeking these rule changes,²¹ but shortly after the Commission issued this *Notice*, Sprint announced that it is partnering with cable companies to offer “Ethernet over DOCSIS . . . via its growing array of access network partners,” and said “we’re confident that once we launch those alternatives we will have 95 percent of the country blanketed with Ethernet access.”²² This partnership underscores that Sprint’s claims about the need for BDS reregulation were misguided or

¹⁹ See, e.g., *Pac. Bell Tel. Co. v. Linkline Commc’ns Inc.*, 555 U.S. 438, 456 (2009); Memorandum Opinion and Order, *Application by SBC Communications Inc., et al. for Authorization to Provide In-Region, InterLATA Services in California*, 17 FCC Rcd. 25650, 25737-25738, ¶¶ 157-59 (2002) (“*SBC Application*”); see also *WorldCom, Inc. v. FCC*, 238 F.3d 449, 458-59 (D.C. Cir. 2001).

²⁰ Of course, if a CLEC believes that an ILEC’s rate is unjust and unreasonable, it can bring a Section 208 complaint with the Commission, but there is no need to adopt new wholesale price rules, which can only harm competition and deter investment.

²¹ Notably, T-Mobile has not even participated in this proceeding and has said BDS is not “our battle to fight” because T-Mobile was “in a good place already.” See TheStreet Transcripts, “T-Mobile US Inc. (TMUS) Earnings Report: Q3 2015 Conference Call Transcript” (Oct. 28, 2015) (“Q3 2015 Conference Call Transcript”), <http://www.thestreet.com/story/13341417/14/t-mobile-us-inc-tmus-earnings-report-q3-2015-conference-call-transcript.html>.

²² Sean Buckley, “Sprint ropes in Ethernet over Copper, Ethernet over DOCSIS into Ethernet strategy,” *FierceTelecom* (May 15, 2016), <http://www.fiercetelecom.com/story/sprint-ropes-ethernet-over-copper-ethernet-over-docsis-ethernet-strategy/2016-05-15>.

disingenuous, and that the *Notice*'s claimed reliance on the transition to 5G is nothing but a fig leaf.

In short, while the Commission may choose to replace its MSA-based framework for assessing BDS competition with a more granular framework, there is no marketplace or data-based rationale for increased regulation of *any* BDS service. There is no case for new regulation of any Ethernet or TDM service with bandwidth above 50 Mbps: Professor Rysman's regression analyses found no evidence of market power for such services. There is no case for regulation of lower capacity Ethernet: Professor Rysman did not report any regressions for such services, but Drs. Israel, Rubinfeld, and Woroch ran those regressions and they show no evidence of market power. There is no case for new regulation of legacy DS1 and DS3 services: Professor Rysman's regressions for these services are fatally flawed and, in any case, the price effects he found are so small as to be immaterial. The Commission's data collection shows that virtually all locations with BDS demand have multiple facilities-based options at all bandwidths, and its own data confirm that non-incumbent providers have won more than half of all BDS revenues. If this proceeding is intended to be a *data-driven* inquiry, then the Commission must heed the data. And the data do not support the kind of mandated price reductions advocated by CLECs and proposed in the *Notice*.

I. THE MARKETPLACE FOR BDS IS ROBUSTLY COMPETITIVE AT ALL LEVELS, AND INCREASED REGULATION OF BDS WOULD BE COUNTERPRODUCTIVE.

There is no basis in the record – and especially not within the 2013 data collection – on which one can legitimately make the case that new regulation of BDS is warranted or desirable. The Commission's data collection shows that BDS customers have multiple facilities-based options in almost all locations where there is demand, and these facts should place an extraordinarily heavy burden on any party seeking to argue that these near-ubiquitous alternative

facilities somehow do not lead to competitive outcomes. The Commission nonetheless seeks comment on what it calls “direct evidence” and other alleged indicia of market power for low-bandwidth BDS services. The principal source of such “direct evidence” relied upon in the *Notice* is Professor Rysman’s study, but that study does not provide evidence of market power; to the contrary, even aside from its flaws, which are significant, it purports to show that competition only reduces prices by 3.2%, an effect that in no way justifies the imposition of a new regulatory regime, particularly one that would threaten to retard investment. The remaining examples of market power “indicia” are makeweights.

A. The Near-Ubiquity of Facilities-Based Alternatives Establishes Beyond Reasonable Dispute That BDS Is Highly Competitive For All Bandwidths.

The *Notice* expressly acknowledges a set of facts and realities concerning the BDS marketplace that must form the starting point for analysis. Taken together, these facts should also be the end of the matter.

First, the *Notice* establishes, contrary to the arguments of some prior commenters, that any analysis of the BDS marketplace must include facilities-based alternatives that are either in or *near* a location with BDS demand. Providers of BDS deploy fiber or other networks in areas where there is demand for BDS, and they build out to individual locations where they win customers. Professor Baker, an economist hired by CLECs, found that competitors typically compete for customers in buildings within about a half mile of their network facilities.²³ Professor Rysman makes similar findings,²⁴ and a “key finding[]” in the *Notice* is that “fiber-

²³ Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593, ¶ 43 (filed Apr. 14, 2016).

²⁴ Rysman White Paper at 218-19 (“a quarter to a half-mile”).

based competitive supply within at least half a mile generally has a material effect on prices of BDS”²⁵

The data collection confirms that the vast majority of buildings with BDS demand are well within these distances. Even as of 2013, about half of these buildings were within 88 feet (0.017 miles) of at least one CLEC’s fiber facilities, 75% were within 456 feet (0.086 miles), 90% were within about 1,107 feet (0.21 miles), and virtually all (98.7 percent) were within a half mile.²⁶ Most of the *demand* (measured by bandwidth) is well within a half mile of competitive facilities: about 98 percent of BDS bandwidth served by AT&T is located in buildings that are less than a half mile from at least one other provider’s network.²⁷ The same is true when the universe is limited to sub-50 Mbps connections: 90% of AT&T’s sub-50 Mbps bandwidth is within a half mile of competitive fiber.²⁸

The *Notice* asks whether there is evidence that two or more non-ILEC competitors are required to achieve competitive results. As explained in Part II below, the answer is clearly no. But even if the Commission were to erroneously conclude that two or more non-ILEC networks are needed to achieve competitive results, the 2013 data still confirm that almost all ILEC demand falls within this category. About 85 percent of AT&T’s demand is in buildings that are *within 1,000 feet of two or more other provider networks*, less than half the distance needed to

²⁵ *Notice* ¶ 161. Moreover, in many instances, competitors are willing to extend laterals even farther. For example, a provider may be willing to build out greater distances if connecting to a customer in the building may lead to winning additional business in other buildings (either nearby or not) or if it obtains a long-term commitment. *Id.* ¶ 212.

²⁶ IRW Second Supp. Decl. ¶ 5.

²⁷ IRW Second White Paper at 5.

²⁸ *Id.*

constrain prices. Eighty one percent are within 800 feet and 75 percent are within 500 feet.²⁹ The same is true for AT&T’s sub-50 Mbps bandwidth services.³⁰

All of the metrics above understate the true extent of competition because they exclude cable companies’ HFC facilities, which are nearly ubiquitous in each cable company’s respective footprint.

Market share data provided in the *Notice* provide further confirmation that competitors have been highly successful in competing for and winning large portions of the BDS marketplace. The *Notice*’s Figure 9 shows that non-ILEC providers earn more in revenues from BDS services than do ILECs. Competitive providers earned \$23 billion of the \$45 billion in BDS revenues for 2013 – and, once again, these figures do not even include cable company revenues.³¹ In addition, Professor Rysman finds that “if we focus on buildings served by fiber, competitive providers are a robust presence, almost the size of ILECs in terms of number of

²⁹ *Id.*

³⁰ *Id.*

³¹ *Notice* ¶ 217, Figure 9. Professor Rysman presents a table with similar results. See Rysman White Paper at 216, Table 1. Professor Rysman suggests that revenues earned from ILEC-affiliated CLECs should be treated as “ILEC” revenue. But this position dramatically distorts competitive realities. As explained by Drs. Israel, Rubinfeld and Woroch, the issue is whether ILECs have market power in their operating territories by virtue of their incumbent status. See IRW Second White Paper at 15, n.6. The data show that ILECs have lost more than half of the marketplace revenues to competitors in their respective regions. It makes no difference whether those competitors are affiliated with ILECs from other regions. Similarly, the *Notice* points out that CLEC retail revenues in this chart include revenues earned from services provided using ILEC-provided special access and UNE services, and raises the question as to whether the retail revenues earned by the CLEC from such services should instead be allocated to the ILEC. The answer is clearly no. One of the main issues in this proceeding is whether ILEC prices for BDS preclude CLECs from using those services to compete against ILECs for retail customers. The revenue shares in this table confirm that CLECs can and do very effectively compete for retail customers using ILEC-provided special access and UNE facilities. *Id.*

buildings served.”³² And the *Notice* points out that six of the top nine providers of Ethernet services, measured by Ethernet port shares, are non-ILECs.³³

The data are thus clear: even as of 2013 non-ILEC providers of BDS had blanketed areas with BDS demand with their own facilities and were using those facilities to compete successfully for BDS customers and revenues.

But even these data do not tell the whole story because metrics that are based on 2013 data dramatically understate the extent of competition *today*. The expansion by non-ILEC competitors since 2013 is well documented in the record.³⁴ For example, the *Notice* correctly points out that in recent years perhaps “[t]he great success story has been that of cable.”³⁵ “Less than a decade ago, cable largely provided no business services of any kind that were materially different from the services marketed to residential customers.”³⁶ More recently, however, “cable began offering BDS services over HFC, as well as fiber, and has forced even the largest incumbent LECs to focus on maintaining market share.”³⁷ In 2013 alone, the data show “that

³² Rysman White Paper at 212.

³³ *Notice* ¶ 83, Chart 1.

³⁴ See, e.g., Comments of AT&T Inc., *Special Access Rates for Price Cap Local Exchange Carriers, AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, at 13-17 (filed Jan. 27, 2016); Comments of Verizon, *Special Access Rates for Price Cap Local Exchange Carriers, AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, at 13-15 (filed Jan. 27, 2016); Comments of CenturyLink, *Special Access Rates for Price Cap Local Exchange Carriers, AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, at 11-25 (filed Jan. 27, 2016) (“CenturyLink Jan. 27 Comments”).

³⁵ *Notice* ¶ 236.

³⁶ *Id.*

³⁷ *Id.*

competitive LECs’ bandwidth grew at six times the growth of the rate of the ILECs.”³⁸ And cable companies have continued to gain more and more market share since 2013. Indeed, a 2015 report found that, over the past two year period, “cable operators have increased the penetration of business locations they serve by more than 50 percent while ILEC penetration dipped nearly 14 percent.”³⁹ Another report found that “cable is the fastest growing segment in the wholesale and retail business Ethernet markets.”⁴⁰

One reason cable companies have been so successful in winning Ethernet customers in the past few years is that they have dramatically extended the reach of their most cutting edge services, including Ethernet with service level agreements (“SLAs”). They have done so by continuing to expand their fiber-based networks to cover millions of additional businesses. And they have rolled out Ethernet services with SLAs over their existing and near-ubiquitous HFC facilities. As a result, cable companies not only offer fiber-based Ethernet services throughout urban areas using their fiber-based facilities, they also offer Ethernet services throughout suburban and rural areas with BDS demand using their HFC facilities. Indeed, Cox “confirms that [BEGIN HIGHLY CONFIDENTIAL] ■ [END HIGHLY CONFIDENTIAL] of its headends” are capable of providing Metro Ethernet services over HFC, and that it offers SLAs with its Ethernet-over HFC product.⁴¹ TWC confirms that “TWC’s Internet access service and

³⁸ *Id.*

³⁹ Sean Buckley, “Cable operators taking greater share of large businesses, says analyst firm” FierceTelecom (Sep. 21, 2015), <http://www.fiercetelecom.com/story/cable-operators-taking-greater-share-large-businesses-says-analyst-firm/2015-09-21>.

⁴⁰ Sean Buckley, “Cord-cutting doesn’t spell doom for cable companies” FierceTelecom (April 7, 2015), <http://www.businessinsider.com/cord-cutting-doesnt-spell-doom-for-cable-companies-2015-7>.

⁴¹ Letter from Michael H. Pryor (Cox Communications) to Marlene H. Dortch (FCC), *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 at 2 (filed May 18, 2016).

Ethernet service are available across all TWC markets, and currently reach, without further construction, [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of business locations within TWC’s footprint.”⁴² TWC’s Ethernet-over-HFC service is also available with SLAs.⁴³ Comcast reports that a significant portion of its headends support Ethernet-over-HFC, and that its Ethernet-over-HFC service includes SLAs relating to availability and speed.⁴⁴ Thus, even if one were to believe that cable HFC facilities in 2013 were used mainly for “best efforts” services that did not compete with ILEC BDS, that is no longer true. Today, HFC facilities are being used to provide Ethernet services with SLAs, which fall squarely within the Commission’s proposed definition of BDS.

Purchasers of BDS confirm the continued growth of competition in BDS in recent years. AT&T has documented that when purchasing services outside of its ILEC territory it is now able to choose from a number of alternative suppliers, including CLECs, cable companies, and fixed wireless providers, and AT&T uses all of these options for both mobile backhaul and for the broadband services it offers to business customers.⁴⁵ CenturyLink and Verizon have provided similar evidence.⁴⁶ T-Mobile, which has not filed comments in this proceeding, announced in August 2012 that it had “upgraded to fiber backhaul over 32,000 cell sites,” which it achieved by working with “dozens of backhaul partners,” which included “cable operators as well as

⁴² Letter from Matthew A. Brill (TWC) to Marlene H. Dortch (FCC), *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (filed Mar. 3, 2016).

⁴³ *Id.*

⁴⁴ See Letter from Matthew A. Brill (Comcast) to Marlene H. Dortch (FCC), *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (filed Mar. 25, 2016).

⁴⁵ See Reply Declaration of Parley C. Casto, attachment B of Reply Comments of AT&T, *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (filed Mar. 12, 2013).

⁴⁶ See, e.g., CenturyLink Jan. 27 Comments at 11-25.

numerous CLECs.”⁴⁷ When asked about T-Mobile’s participation in this proceeding, T-Mobile’s CTO explained that BDS was not “our battle to fight” because T-Mobile was “in a good place already.”⁴⁸

Even some of the most vocal proponents of BDS regulation admit that there are in fact an increasingly wide variety of competitive options for BDS. For example, although Sprint continues to decry the supposed lack of competitive alternatives to ILEC BDS and argues that cable offerings are not substitutes for ILEC BDS, Sprint recently announced to the press that it is partnering with cable companies to offer “Ethernet over DOCSIS . . . via its growing array of access network partners,” and Sprint’s Vice President and General Manager of Sprint’s Global Wireline Business Unit explained that “we’re confident that once we launch those alternatives we will have 95 percent of the country blanketed with Ethernet access.”⁴⁹

On this record, there is clearly robust competition for BDS services at all levels. It is thus critical that any regulation of BDS be limited to the increasingly small portion of the marketplace where competition is still lacking (and likely to remain lacking for the foreseeable future).

B. The Commission Cannot Rely on the Rysman Paper as Evidence Of Market Power For DS1 and DS3 Services.

The *Notice*’s main source of “evidence” of ILEC market power are the results of regression analyses presented in a White Paper submitted by Professor Rysman. The theory underlying these regressions is that, as an economic matter, it can be presumed that ILECs have

⁴⁷ Phil Goldstein, “T-Mobile to focus on 1900 MHz LTE deployment to expand network footprint,” FierceWireless (Sep. 24, 2014), <http://www.fiercewireless.com/story/t-mobile-focus-1900-mhz-lte-deployment-expand-network-footprint/2014-09-24>.

⁴⁸ See Q3 2015 Conference Call Transcript.

⁴⁹ See Sean Buckley, “Sprint ropes in Ethernet over Copper, Ethernet over DOCSIS into Ethernet strategy,” FierceTelecom (May 15, 2016), <http://www.fiercetelecom.com/story/sprint-ropes-ethernet-over-copper-ethernet-over-docsis-ethernet-strategy/2016-05-15>.

market power for DS1 and DS3 services if the regressions show that ILEC prices are lower in areas where competitive providers have entered. Accordingly, Professor Rysman uses the 2013 data to perform regressions that compare ILEC DS1 and DS3 prices in buildings where competitors have deployed connections or nearby facilities with those where they have not done so. These regressions purport to show that ILEC prices are lower in buildings where competitive providers have deployed facilities than they are elsewhere.

The *Notice* asks whether these regressions are valid indicators of ILEC market power for DS1 and DS3 services. They are not. Drs. Israel, Rubinfeld, and Woroch have reviewed these regression analyses and demonstrate that they do not establish a causal relationship between ILEC prices in a building and the number of competitors that can serve the building. Equally important, however, *even if* Professor Rysman’s study were valid, the effect he shows is so small that the costs and burdens of any new regulation of such services would far outweigh whatever negligible benefits such new regulations might provide.

1. The Rysman Regression Analyses Are Not Reliable.

It is important to emphasize at the outset that Professor Rysman’s results relate solely to legacy TDM DS1 and DS3 services. Professor Rysman specifically tested and found *no support* for the proposition that ILECs have market power for *any* services (Ethernet or TDM) above 45 Mbps. Although he did not report regressions for Ethernet services below 45 Mbps, as explained below,⁵⁰ application of his regressions to those services also shows that ILECs have no market

⁵⁰ Rysman White Paper at 229 (“The effect for high-bandwidth lines is statistically insignificantly different from zero for census tract fixed effects and is positive for county fixed effects.”); *id.* at 201 (“[R]egressions for higher bandwidth lines [higher than DS3s] show muddled and conflicting effects of competition, often at low levels of statistical significance.”); *id.* (“Competitive providers are a robust presence for services above 45 Mbps, almost the size of ILECs in terms of number of buildings served.”).

power. Nonetheless, even with that limited scope, Professor Rysman’s regressions do not establish that ILECs have market power even for the DS1 and DS3 services that were examined.

As Drs. Israel, Rubinfeld, and Woroch explain, regression analyses using the 2013 data set cannot be used to accurately isolate the effect of competitive entry on ILEC prices. In econometrics terms, there is an “endogeneity” problem, which is essentially a correlation/causation problem. To the extent regression analyses indicate that lower ILEC prices may be *correlated* to some degree with competitive entry, such regressions do not establish that they are *caused* by competitive entry. That is because any observed correlation could instead be due to the fact that competitors tend to enter in areas where prices will naturally be lower due to other conditions, such as favorable economic conditions (*e.g.*, lower costs and higher revenue opportunities).⁵¹

Professor Rysman acknowledges this issue. He correctly explains that a “major concern” with attempting to use the 2013 data to test whether competitive entry is causing lower ILEC prices is that “locations may differ in how costly they are to serve with BDS” and thus “low cost areas might see low prices and high competition *independent of any causal effect* of competition on price.”⁵² Similarly, locations “differ in their regulatory status, . . . and locations differ to the extent they face competition from outside the BDS market, such as from best efforts cable.”⁵³

As explained by Drs. Israel, Rubinfeld, and Woroch, there are multiple econometric techniques that can be used to filter out the unwanted correlations, leaving only the effects that the econometrician is examining. But the data here lack the necessary elements to implement these techniques. Professor Rysman uses one of them anyway. Specifically, he uses “fixed

⁵¹ IRW Second White Paper at 7-17.

⁵² Rysman White Paper at 227 (emphasis added).

⁵³ *Id.*

effects” statistical techniques. But, as Drs. Israel, Rubinfeld, and Woroch further explain, fixed effects techniques cannot effectively address the endogeneity issues in this instance. The goal is to filter out any effects on ILEC prices caused by cost, demand, revenue opportunities and other economic conditions, thus isolating the effects on price caused by competitors who have deployed competing facilities. Professor Rysman attempts to filter out these other effects at the census tract and county levels. But that approach cannot account for different economic conditions that occur within those census tracts and counties. If observed ILEC prices are driven by different economic conditions between two census blocks (census tracts are comprised of several census blocks), the fixed effects technique would not filter out those effects, because the fixed effects techniques are filtering only the effects of different economic conditions across census *tracts* (or counties).⁵⁴

A simple example illustrates the problem. Suppose there are two census blocks. In one census block, the buildings are closer to the ILEC’s central office. In the other census block, the buildings are farther from the ILEC’s central office. The ILEC’s average price in the first census block will generally be lower, because, for example, the circuits will require less mileage. If there happens to be a competitor in the census block where buildings are closer to the ILEC’s central office, the regressions performed by Professor Rysman would erroneously conclude that the existence of the competitor is causing the lower price, and not the different economic conditions between the two census blocks. The fixed effects techniques used in Professor Rysman’s regressions can partially account for this difference if the census blocks are located in *different census tracts*, but not if they are located in the same census tract.⁵⁵

⁵⁴ IRW Second White Paper at 7-17.

⁵⁵ *See id.* at 7-19.

Professor Rysman acknowledges this problem, noting that his “approach [using fixed effects techniques] is problematic to the extent that unobserved effects differ across census blocks within the same census tract.”⁵⁶ Indeed, he acknowledges that “it is impossible to completely control for unobserved cost and demand heterogeneity,” and thus it is “possible that low cost areas attract competitive entry, which leads to a spurious correlation between competition and price.”⁵⁷ As Drs. Israel, Rubinfeld, and Woroch explain, these issues render the regression results irretrievably biased, and therefore the Commission cannot rely on them.⁵⁸

For these reasons, it is impossible for the Commission to conclude from Professor Rysman’s regressions that any correlation between competitive entry and ILEC prices is a causal relationship. These regression analyses thus provide no legitimate basis for concluding that ILECs have market power.

As detailed in the White Paper submitted by Drs. Israel, Rubinfeld, and Woroch, there also are *other* significant problems with the regression analyses presented by Professor Rysman (many of which he correctly acknowledges). The purpose of the regressions is to draw inferences about ILEC prices from competitive entry. Therefore, it is critical that the underlying data are accurate for both prices and competitive entry. As Drs. Israel, Rubinfeld, and Woroch show, that is not the case. For example, the data used in the regressions include DS1 prices that are as high as \$116,353 (DS1s generally cost about \$200-\$400).⁵⁹ In addition, the pricing data used in the regressions excluded circuits that do not have the same bandwidth for all components

⁵⁶ Rysman White Paper at 228; *see also id.* (“For instance, it might be the unobserved costs of providing service varies substantially even within census tracts” or that “the ability of cable operators to provide alternatives to BDS . . . varies across census blocks”).

⁵⁷ *Id.* at 232 (fixed effects approach can only “mitigate” but not solve the problem).

⁵⁸ IRW Second White Paper at 7-17.

⁵⁹ *See id.* at 18.

(e.g., channel termination and local transport), and thus systematically exclude lower priced circuits that rely on multiplexing (e.g., a DS3 transport facilities multiplexed to DS1 channel terminations).⁶⁰ The data also exclude about 42 percent of buildings, and those exclusions are not random.⁶¹ Thus, the regressions are based on a very distorted set of underlying data.⁶²

2. The Effects Rysman Shows Are Too Small to Justify New Regulation.

Even ignoring the problems with Professor Rysman’s analysis (many of which he concedes), and accepting the results in the regressions at face value, those results show that the impact of competition on DS1 prices at the census tract level is generally very small. For example, Table 14 shows that a competitor with a connection to a building will cause the ILEC to reduce prices by only 3.2 percent. Professor Rysman concedes that this figure is “not especially large by the standards of competition analysis;”⁶³ in fact, it would not even be considered evidence of market power under the Justice Department’s well-established “SSNIP” test (which has a 5 percent cut-off). That being the case, Professor Rysman’s analysis fails to document any problem that warrants regulatory intervention.⁶⁴ But even the exceedingly small

⁶⁰ *See id.* at 18-19.

⁶¹ *See id.* at 19.

⁶² Moreover, application of additional econometric techniques raises questions as to whether many of the results are statistically significant. There are multiple methods for computing standard errors, on which tests for statistical significance are based. As explained by Drs. Israel, Rubinfeld, and Woroch, given the nature of the data being analyzed here, the best method for computing the standard error in this case is arguably a “clustered” standard error. When standard errors are computed using that method (rather than ordinary standard errors reported with Professor Rysman’s regressions), the regressions show no statistically significant results for DS3 services. *Id.* at 19-20.

⁶³ Rysman White Paper at 228-29.

⁶⁴ Under the Administrative Procedure Act, agencies may not impose complex regulatory “solutions” to problems that are not substantiated or material. *See, e.g., Nat’l Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 843 (D.C. Cir. 2006) (“Professing that an order ameliorates a real industry problem but then citing no evidence demonstrating that there is in fact an industry problem is not reasoned decision-making.”); *Associated Gas Distribs. v. FERC*, 824 F.2d 981,

price difference posited by Professor Rysman’s analysis overstates the case because, for the reasons stated above, this figure is picking up cost-based and other effects that will themselves drive lower prices, independent of competitive entry. To conclude that ILECs have market power for DS1 services based on regressions showing a price difference of *at most 3.2%* – especially given the flaws in the data themselves used in the analysis – would be arbitrary in the extreme.

Moreover, any benefits from erecting a complex scheme of regulation merely to address such small competitive effects would be far outweighed by the enormous costs of such regulations. As the Supreme Court recently explained in *Michigan v. EPA*,⁶⁵ cost-benefit comparisons are essential to reasoned decisionmaking: “Agencies have long treated cost as a centrally relevant factor when deciding whether to regulate. Consideration of cost reflects the understanding that reasonable regulation ordinarily requires paying attention to the advantages *and* the disadvantages of agency decisions.”⁶⁶

Here, the costs and burdens of the Commission’s proposed regime could be enormous. For example, AT&T’s access billing systems today are set up to bill by MSA, in accordance with the rules that have been in place for many years. Regulatory changes that would effect more granular geographic classifications, would require large investments to adapt those systems to the far more complex set of rules proposed here, and would likely take 18-24 months to accomplish.

1019 (D.C. Cir. 1987) (agency lacks any basis for fashioning “an industry-wide solution for a problem that exists only in isolated pockets,” and “the disproportion of remedy to ailment” is therefore arbitrary and capricious).

⁶⁵ 135 S. Ct. 2699 (2015).

⁶⁶ *Id.* at 2707 (emphasis in original); *see also id.* (“[n]o regulation is ‘appropriate’ if it does significantly more harm than good”).

In addition, as Drs. Israel, Rubinfeld, and Woroch have explained, *ex ante* regulation inherently imposes burdens on competition, and the Commission’s heavy-handed proposals run a considerable risk of over-regulation and unintended consequences. Indeed, the Commission has repeatedly emphasized that one of its most important priorities is to encourage broadband investment, but rules designed to aggressively lower the prices of legacy DSn services – and to pile new regulations onto broadband services – directly undermine that priority. The Commission has no valid justification for risking such harm to the IP transition in a vain attempt to chase such negligible “benefits” as they relate to a set of services that carriers are in the process of retiring. Under any reasonable calculus, these concrete and substantial harms outweigh the dubious benefits of reregulation of BDS.

C. The Commission’s Remaining “Indicia” of Market Power Are Makeweights.

The *Notice* contains several additional examples of what the Commission calls “indicia” of market power, but the facts refute each of these claims.

Headroom. The *Notice* presents tables showing that ILECs have had a small amount of “headroom” (in percentage terms) under the price caps for DS1 and DS3 services since 2012, and expresses the view that “the fact that the price capped incumbent LECs have kept their prices at the top of the cap is additional evidence of market power.”⁶⁷ That view is illogical and insupportable.

The mere fact that rates are near the price cap ceilings set by the Commission would be indicative of market power only if those ceilings were above the price that would exist in a competitive market.⁶⁸ But the Commission has made no such finding.⁶⁹ Rather, as explained in

⁶⁷ *Notice* ¶ 239.

⁶⁸ See IRW Second White Paper at 21-22.

detail below, *see* Section IV.C *infra*, the evidence in this proceeding overwhelmingly establishes that the existing caps are *not* above competitive levels, and that no downward adjustment of today’s price caps is warranted. Accordingly, the fact that today’s pricing might be at or near the cap should not be surprising or of concern. It certainly provides no basis for any conclusions about market power.

ILEC-Affiliate Out-of-Region Facilities. The *Notice* states that ILEC-affiliated CLECs “have engaged in limited facilities-based investment relative to certain other [CLECs] and in some areas have avoided the use of UNEs.”⁷⁰ The *Notice* does not cite to any evidence that ILEC-affiliated CLEC investment is relatively low, nor does it explain why, even if true, this observation constitutes “direct evidence” that ILECs have market power in any particular geographic area or for any service.

In fact, to extent the Commission’s suppositions about ILEC out-of-region investment are true, they prove absolutely nothing. ILECs do not have unlimited resources, and their investments reflect business decisions about the best way to utilize those limited resources. Given this reality, the most obvious inference that could be drawn from any purported lack of facilities-based investment out-of-region by ILECs is that wholesale prices are sufficiently low such that the ILECs choose to direct their limited resources to other business opportunities. That inference is far more plausible than the Commission’s counter-intuitive suggestion that ILECs would forgo investing in their own facilities notwithstanding supracompetitive pricing for

⁶⁹ The current price caps are presumed to be just and reasonable under Section 201 of the Act pursuant to the Commission’s existing incentive regulation scheme. Notice of Proposed Rulemaking, *Comprehensive Review of the Part 32 Uniform System of Accounts*, 29 FCC Rcd. 10638, 10640-10641, ¶ 6 (2014) (“Price cap regulation is a form of incentive regulation that relies on a series of Price Cap Indexes (PCIs) to limit the prices carriers charge for services to levels that are *presumed to be just and reasonable*.” (emphasis added)).

⁷⁰ *Notice* ¶ 243.

wholesale inputs. In fact, it is underscored by the *Notice* itself which acknowledges that ILECs' out-of-region CLECs are among the larger and more successful CLECs in terms of revenues. If it is true that this success is based on the use of special access facilities purchased from the in-region ILEC (or from other suppliers), then this finding dramatically *undercuts* any suggestion that ILEC special access prices, terms or conditions are somehow precluding successful competition and any claim that ILECs have or can exercise market power.⁷¹

Barriers to Entry. The *Notice* seeks comment on CLEC claims that there are unique barriers to entry for customers with demand for only DS1 and DS3 services, and thus the Commission should conclude that ILECs have market power for those services.⁷² In support of these assertions, the CLECs have provided only anecdotal evidence and lists of the costs incurred when building out such facilities.

In fact, the data show that CLECs can and do routinely compete for these lower-bandwidth customers. The 2013 data show that well over half of the buildings served by CLECs have bandwidth equal to 45 Mbps or less.⁷³ There is thus no merit to the CLECs' self-serving assertions that they cannot deploy such facilities – the data show that they clearly can and do.

⁷¹ See also IRW Second White Paper at 20. Although the *Notice* does not cite any data supporting this assertion, it may be relying on the metric reported by Professor Rysman that ILEC-affiliated CLECs account for less than 7% of all connections, whereas non-affiliated CLECs account for 25% of all connections. There are many more non-affiliated CLECs than ILEC-affiliated CLECs, which should explain much of the apparent difference in investment. In all events, this assertion clearly does not apply to AT&T. AT&T has made substantial investments in facilities operated by its affiliated CLEC networks in virtually every major metropolitan area outside of its ILEC territory.

⁷² See *Notice* ¶¶ 224-36.

⁷³ IRW Second White Paper at 23.

Concentration Metrics. The *Notice* contains a section entitled “Concentration by Any Measure Appears High in This Industry,”⁷⁴ but the data contained in that section do not support that assertion. Indeed, the lead metric in this section is the claim that ILECs are the only provider with a connection to about 77 percent of buildings with special access demand, but as the Commission itself recognizes, competition occurs between providers that are in *or reasonably near* a given building. As explained above, once nearby competitors are included, the data confirm that customers in the vast majority of buildings have multiple facilities-based options. Indeed, even if building-connection metrics were relevant, the data presented in the *Notice* show that most buildings are served by multiple competitors. The *Notice* correctly recognizes that Ethernet services offered by cable companies over their HFC network are part of the BDS marketplace, and when cable HFC building connections are taken into account, the portion of ILEC-only buildings falls to only about 14%, according to the Commission Staff’s analysis.⁷⁵ Moreover, as noted, the *Notice’s* data show that ILECs’ in-region BDS revenues account for significantly less than half of all BDS revenues – which further confirms that the BDS marketplace is not highly concentrated.⁷⁶

5G Wireless. The *Notice* suggests that regulation of BDS may be justified because it is expected to be an important input for 5G wireless services. The industry is still in the early stages of determining the standards for and testing 5G technology, but one thing is clear: the wireless industry is not going to be using legacy DS1s and DS3s for backhaul. The completion of the 5G standards-setting process and the widespread deployment and adoption of 5G is scheduled to coincide early in the next decade with the *retirement* of the legacy networks used to

⁷⁴ *Notice* ¶¶ 216-223.

⁷⁵ *See Notice* ¶ 221, Table 4.

⁷⁶ *Id.* ¶ 217, Figure 9.

provide the DS1 and DS3 services at issue here. Indeed, the wireless industry has *already* transitioned their backhaul needs to Ethernet, and 5G backhaul is likely to be a combination of Ethernet fiber services and the re-use of wireless spectrum. Thus the development of 5G cannot serve as an excuse to regulate TDM services. And to the extent that 5G backhaul increases demand for Ethernet-based backhaul, that only creates new opportunities for the numerous providers already competing in that space and others who might want to enter. Notably, as discussed below, there is *zero* evidence in the record of any market power in the Ethernet marketplace and thus no corresponding need for regulation of Ethernet services for 5G.

Suggestions that new intrusive regulation of BDS is needed to facilitate wireless carriers' transition to 5G are further refuted by other marketplace facts. As noted above, in direct contravention of its claims, Sprint has announced that it is partnering with cable companies to offer "Ethernet over DOCSIS . . . via its growing array of access network partners" and that it is "confident that once we launch those alternatives we will have 95 percent of the country blanketed with Ethernet access."⁷⁷ Similarly, T-Mobile has chosen to not participate in this proceeding, explaining that BDS is not "our battle to fight" because T-Mobile was "in a good place already."⁷⁸

II. THERE IS NO BASIS FOR REGULATION OF ETHERNET SERVICES.

There is no basis whatsoever for imposing new *ex ante* rate regulations on Ethernet services. The Commission expresses concern that providers might be able to charge supra-competitive rates for Ethernet services in areas the Competitive Market Test deems to be "non-

⁷⁷ Sean Buckley, "Sprint ropes in Ethernet over Copper, Ethernet over DOCSIS into Ethernet strategy," FierceTelecom (May 15, 2016), <http://www.fiercetelecom.com/story/sprint-ropes-ethernet-over-copper-ethernet-over-docsis-ethernet-strategy/2016-05-15>.

⁷⁸ See Q3 2015 Conference Call Transcript.

competitive.”⁷⁹ To combat this hypothetical possibility, the Commission seeks comment on various types of “anchor” or “benchmarking” mechanisms that would act as “guidance as to the range of rates” for such services.⁸⁰ In fact, the record shows that the marketplace for Ethernet services is intensely competitive and the *Notice* does not point to any evidence to the contrary. Thus, there is no legitimate basis on which the Commission could impose any new regulation on Ethernet services in this proceeding.

First, the Commission would face a high legal bar in adopting any new regulation of Ethernet. The Commission granted forbearance from *ex ante* rate regulation for Ethernet services almost a decade ago, and the D.C. Circuit affirmed those rulings.⁸¹ The Commission granted this relief because it found that “there are a myriad of providers prepared to make competitive offers to enterprise customers demanding packet-switched data services located both within and outside any given incumbent LEC’s service territory,” including “many competitive LECs, cable companies, systems integrators, equipment vendors, and value-added resellers.”⁸² For that reason, the Commission granted forbearance from all *ex ante* rate regulation, including dominant carrier regulation, tariff filing, and cost support requirements, although it made clear that Sections 201 and 202 and the Section 208 complaint process would continue to apply.⁸³

⁷⁹ *Notice* ¶ 420.

⁸⁰ *Id.*

⁸¹ *AT&T Title II and Computer Inquiry Forbearances*, 22 FCC Rcd. 18705 (2007), *aff’d*, *Ad Hoc Telecomms. Users Comm. v. FCC*, 572 F.3d 903 (D.C. Cir. 2009).

⁸² *Id.* at 18718-19, ¶ 22.

⁸³ *Id.* at 18715-33, ¶¶ 17-51.

The Commission has never purported to undo or re-impose regulation where there has been forbearance under Section 10 of the Communications Act.⁸⁴ And the standard for re-imposing regulation that the Commission previously abandoned would be very high, because any reversal of course here would have to turn on a material change in the Commission’s view of the facts as compared to its prior forbearance orders. Established Supreme Court precedent requires that when an agency adopts “new policy” which “rests upon factual findings that contradict those which underlay its prior policy,” it must “provide a more detailed justification than what would suffice for a new policy created on a blank slate.”⁸⁵ Accordingly, the Commission would have to provide an especially “detailed justification” showing that regulatory intervention is affirmatively necessary in light of changed circumstances, *i.e.*, that the Commission’s finding in 2007 that the Ethernet market is highly competitive is no longer valid. Such a showing would not be possible, however, because the 2013 data collection confirms that the market is robustly competitive. Indeed, the record shows that there is far *less* justification for *ex ante* price regulation now than when the Commission granted forbearance in 2007.

As an initial matter, there are no “incumbent” providers for Ethernet. When Ethernet first became available, no provider had an Ethernet network, including the incumbent LECs, and thus all carriers were starting from scratch with no incumbent advantage. Over the past decade or more, a wide variety of companies, including ILECs, CLECs, cable companies, and others, have invested billions of dollars to deploy Ethernet services for their customers. The result is that

⁸⁴ 47 U.S.C. § 160. Austin Schlick, FCC General Counsel, *A Third-Way Legal Framework for Addressing the Comcast Dilemma*, at 9 (May 6, 2010), http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-297945A1.pdf (“The difficulty of overcoming section 10’s deregulatory mandate and a prior agency finding in favor of forbearance is illustrated by the fact that the FCC has never reversed a forbearance determination made under section 10, nor one made for wireless under the similar criteria of section 332(c)(1).”).

⁸⁵ *Fox Television*, 556 U.S. at 515; *see also id.* (“[A] reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy.”).

there are dozens of non-ILEC providers of Ethernet services, and no provider has a port share that exceeds one-fifth of the market.⁸⁶ Indeed, there are nine providers with port shares of four percent or more, including three CLECs, and three of the nation’s largest cable companies.⁸⁷ Further, one of the CLECs that has been the most incessant complainer in this proceeding, Level 3, is the second largest Ethernet provider in the U.S. measured by port share.⁸⁸ Time Warner Cable has been described as a “significant mover in the league” and Comcast “continues to expand its fiber and Ethernet reach.”⁸⁹ Other providers – *i.e.*, those with port shares under 4 percent – together have, in the aggregate, port share in excess of 20 percent.⁹⁰

The data collected and analyzed in this proceeding further confirm that no Ethernet provider has market power. The CLECs’ consultants’ own analyses of the 2013 data collection show that non-ILECs’ share for services ranging from 50 Mbps and higher (which includes Ethernet services), as of 2013, was almost 50 percent measured by circuit counts and over 41 percent measured by revenue.⁹¹ And non-ILECs have continued to expand rapidly. Indeed, the 2013 data collected by the Commission indicates that non-ILECs have been growing at a much faster rate than ILECs. As explained in the *Notice*, “[c]omparing January 2013 to December 2013 billing information from the [2013 Data] *Collection*, the bandwidth of Ethernet circuits

⁸⁶ See Ethernet LEADERBOARD.

⁸⁷ See *id.*

⁸⁸ *Id.*

⁸⁹ Zacks Equity Research, “Cable MSOs Challenge Telecom Providers in Ethernet Market” (Mar. 10, 2016), <https://www.zacks.com/stock/news/210120/cable-msos-challenge-telecom-providers-in-ethernet-market> (noting that Time Warner Cable “gained 14.4% in business revenues in 2015 driven by increases in high-speed data and voice subscribers” and Comcast “registered 20% growth year over year in 2015”).

⁹⁰ See Ethernet LEADERBOARD.

⁹¹ Declaration of William P. Zarakas and Susan M. Gately, Appendix C, Tables 2 & 3, attached to the Comments of Sprint Corp., *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM 10593 (filed Jan. 27, 2016).

provisioned by incumbent LECs grew by 5.3 percent, and those provisioned by competitive providers grew by 31.6 percent.”⁹² Such asymmetrical growth is incompatible with the notion that ILECs have market power over Ethernet services.⁹³ Moreover, Professor Rysman used his regression analyses expressly to test for market power for Ethernet and other services that have traditionally provided higher bandwidth, and found no such evidence.⁹⁴

Given the total lack of evidence of market power for Ethernet services, the *Notice* suggests (at least implicitly) that carriers may have market power for lower-band Ethernet services that might justify new regulation. But again, there is no record evidence to support that conclusion. Indeed, Professor Rysman did not even attempt to analyze low-band Ethernet services: “[d]ue to timing constraints, the data set analyzed did not include packet-based services with bandwidths of 45 Mbps and less.”⁹⁵ Drs. Israel, Rubinfeld, and Woroch, however, did conduct those regressions, and the results show that ILEC prices for packet based services do not decline in response to competition (indeed, the results show that competitive Ethernet entry causes price *increases*).⁹⁶ In other words, using the same approach to measuring market power used in the Rysman analyses, the data show that there is no evidence of market power for low band Ethernet services. Moreover, there is no evidence that any type of carrier has an inherent

⁹² *Notice* ¶ 81. See also IRW Second White Paper at 25 (citing IRW White Paper at 24).

⁹³ See IRW Second White Paper at 25.

⁹⁴ Rysman White Paper at 229; *Notice* ¶ 244.

⁹⁵ Rysman White Paper at 226 n.31.

⁹⁶ IRW Second White Paper at 26 (“[w]e selected ILEC circuits that were packet-based and that had a bandwidth less than 45 Mbps. Using the resulting sample of about 40,000 circuits, we estimated Professor Rysman’s “base model” which includes an indicator for one or more competitors with a special access connection in the same block (Table 14). The regression estimated a 4.1% *increase* in ILEC price of this type of circuit when there was a facilities competitor in the block, and that increase was highly statistically significant. If one were to adopt Professor Rysman’s methodology, this result would reject a claim that ILECs exercise market power for low-band, packet-based circuits.”).

competitive advantage in the deployment of lower-band Ethernet services, or that any entity is exercising market power over lower-band services.

Nonetheless, the *Notice* appears to *assume* market power for Ethernet services that provide bandwidth of 45 Mbps or lower by bootstrapping its flawed assumption of ILEC market power for DS1 and DS3 services. But that assumption (like the Commission’s assumptions about DS1 and DS3 services) is ungrounded because, as noted, actual regressions using the same methodology as the Commission’s chosen economist show that ILECs do *not* have market power in any Ethernet services, regardless of bandwidth.⁹⁷ Indeed, even if (contrary to fact) there were valid evidence that ILECs have market power over legacy TDM-based DS1 and DS3 services, it does not follow that ILECs have market power over Ethernet services, which is the replacement product for those legacy TDM-based services. There are numerous competing providers for lower-bandwidth Ethernet services, with cable companies and CLECs being among the largest. And as shown above, CLECs have deployed sub-50 Mbps connections to many locations, and most of those locations have less than 50 Mbps of demand in the aggregate.

In short, re-regulation of Ethernet services would flunk the basic requirement of reasoned decisionmaking that the Commission “examine the relevant data and articulate a satisfactory explanation for its action.”⁹⁸ The Commission’s rules must have a factual basis,⁹⁹ and they must

⁹⁷ See IRW Second White Paper at 26.

⁹⁸ *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29, 43 (1983).

⁹⁹ *Id.* (“[A]gency must examine the relevant data and articulate a satisfactory explanation for its action, including a rational connection between the facts found and the choice made” (quotation omitted)); see also *id.* (“[n]ormally, an agency rule would be arbitrary and capricious if the agency . . . offered an explanation for its decision that runs counter to the evidence before the agency”).

also account for trends and developments in the data¹⁰⁰ – which means here that the Commission must adequately account for the ongoing explosive growth of CLEC and cable-provided Ethernet services.¹⁰¹ Particularly insofar as the Commission is using a data set that is already three years old, it is particularly imperative that it be cognizant, not only of changes that have taken place in the past three years, but those that are ongoing and can be expected to continue reshaping the marketplace in the years to come. Since even the increasingly stale data reflecting 2013 deployment levels fails to support a finding that ILECs have market power in Ethernet, there is no possible basis upon which the Commission could conclude otherwise now.

Accordingly, the Commission should affirm its tentative proposal to continue forbearing from tariffing requirements for Ethernet services, and should reject its various benchmarking proposals. Absent any record evidence that Ethernet services are priced above competitive levels, those proposals are wholly unnecessary. Benchmarking Ethernet rates to TDM rates also would be inherently arbitrary. As the Commission notes, there cannot be a mechanical one-to-one correspondence between TDM and Ethernet services that would allow the Commission to

¹⁰⁰ *Dist. Hosp. Partners, L.P. v. Burwell*, 786 F.3d 46, 57 (D.C. Cir. 2015) (“[A]n agency cannot ignore new and better data” (emphasis in original)); *Butte Cnty v. Hogen*, 613 F.3d 190, 194 (D.C. Cir. 2010) (“an agency’s refusal to consider evidence bearing on the issue before it constitutes arbitrary agency action within the meaning of § 706”); *Catawba Cnty., N.C. v. EPA*, 571 F.3d 20, 46 (D.C. Cir. 2009) (agencies “have an obligation to deal with newly acquired evidence in some reasonable fashion” (quoting *Am. Iron & Steel Inst. v. EPA*, 115 F.3d 979, 1007 (D.C. Cir. 1991))).

¹⁰¹ See, e.g., *Comcast Corp. v. FCC*, 579 F.3d 1, 7 (D.C. Cir. 2009) (vacating Commission rule that capped the market share of any single cable television operator at 30% of subscribers because the Commission “fail[ed] to consider the impact of [direct broadcast satellite] companies’ growing market share” and “the growth of fiber optic companies”); *Ill. Pub. Telecomm. Ass’n v. FCC*, 117 F.3d 555, 564 (D.C. Cir. 1997) (vacating Commission rates for certain types of payphone calls because the Commission “failed to respond to any of the data showing that the costs of different types of payphone calls are not similar”); *Natural Res. Defense Council v. Herrington*, 768 F.2d 1355, 1391 (D.C. Cir. 1985) (agency may not “continue to rely on the market penetration algorithm and the ORNL model if further study in light of more complete information shows the model’s prediction to be unreliable”).

use TDM service rates themselves as a benchmark. Rather, the Commission would have to adopt some sort of conversion factor to establish the guidelines.¹⁰² But the *Notice* provides almost no detail about precisely how it would calculate or apply such factors, and that process would present considerably greater difficulties than the *Notice* would suggest. The rates a customer may pay for a DS1 or DS3 can vary with mileage and other factors (such as service configuration), and thus there is no obvious answer as to what “rate” the Commission would use as the basis for its conversion factor. Indeed, any such rigid “bit-rate” conversion factor would be inherently arbitrary, in light of the fact that Ethernet involves significantly different capabilities, flexibilities, and pricing structures (*e.g.*, non-distance-sensitive pricing).

For these reasons, if the Commission nonetheless adopts a benchmarking proposal, it should emphasize (as the *Notice* itself proposes) that such benchmarks would not have the force of price caps, but rather would function merely as a nonbinding guide post that could inform marketplace negotiations or serve as a safe harbor in complaint proceedings.¹⁰³ Even as such, it is critical that the limitations of any benchmarks be recognized; otherwise carriers might find themselves without adequate leeway to cover their costs, particularly for low-band Ethernet services requiring newly constructed connections. As the Commission proposes, section 208 complaints would be resolved not by rigid application of any benchmark, but “based on the facts before [it] in each individual circumstance,” and “providers of Ethernet BDS could make

¹⁰² *See, e.g., Notice* ¶ 430 (“For example, the anchor price for a particular market for a 5 Mbps Ethernet service would be the cost of the closest TDM equivalent offered by the incumbent LEC, which, for example, might be a DS1. This would not imply that the price of the Ethernet service should be the same as that of the nearest equivalent service, but only that the Commission would judge whether the 5 Mbps service price was just and reasonable in the light of the DS1 price. In this example, the Commission could determine that the 5 Mbps service price should not exceed the price of the DS1 multiplied by 3.3 (= 5/1.5) . . .”).

¹⁰³ *Notice* ¶ 420 (“the proposed methodology is not prescriptive, and is intended to facilitate providers and customers negotiating reasonable commercial agreements”).

arguments about why the services at issue cost more to provide than the TDM services to which we would look to benchmark prices.”¹⁰⁴

Finally, the Commission should not require Ethernet providers to publish their generally available rates.¹⁰⁵ Carriers routinely negotiate Ethernet rates with their customers, often as part of a larger agreement that may contain a variety of concessions on different issues. The ability to negotiate such agreements, which are tailored to the interests of the customer, is manifestly in the public interest. Customers and carriers alike, however, typically consider the details of these agreements to be commercially sensitive, and mandated public disclosure of generally available rates would inhibit the negotiation process.

III. ANY NEW COMPETITIVE MARKET TEST MUST ACCOUNT FOR ALL SOURCES OF COMPETITION, BE SIMPLE TO ADMINISTER, AND SUPPORTED BY DATA.

The Commission seeks comment on how to design a new “Competitive Market Test” that would demarcate areas where the BDS marketplace is “competitive” and “non-competitive.”¹⁰⁶ Although the *Notice* acknowledges that any such test must be administratively feasible and commercially practical to implement,¹⁰⁷ the *Notice* nonetheless suggests an inordinately complex test focused on the number of providers in extremely small, geographically granular marketplace areas (*e.g.*, census blocks) coupled with additional possible “factors” such as “bandwidth, different customer classes, [and] business density.”¹⁰⁸

¹⁰⁴ *Id.* ¶ 440.

¹⁰⁵ *See id.* ¶ 436.

¹⁰⁶ *Notice* ¶ 270. As noted, the *Notice* presents no evidence of market power for BDS with bandwidth above 45 Mbps in any circumstances, and thus there would be no record basis for regulating any BDS above 45 Mbps even in the areas a Competitive Market Test would deem “non-competitive.”

¹⁰⁷ *Id.* ¶ 280.

¹⁰⁸ *Id.* ¶ 271.

To the extent the Commission chooses to implement a more granular Competitive Market Test, there is a much simpler way. As the Commission acknowledges, any test of this type must rely on proxy metrics to be administratively feasible.¹⁰⁹ In contrast to its prior efforts, however, the Commission today has the ability to use the comprehensive dataset it has collected to double-check how well its chosen proxy corresponds to the presence of alternative facilities and the availability of competitive options in the marketplace. Using the Commission’s data, Drs. Israel, Rubinfeld, and Woroch have developed a very simple proxy test, based on census tracts instead of MSAs, for services 45 Mbps and below. Under this test, a census tract should be deemed “competitive” for services offering 45 Mbps or lower bandwidth if two or more providers have deployed facilities in or within 2,000 feet of that census tract.¹¹⁰ As explained below, the IRW Second White Paper demonstrates that this test constitutes an accurate proxy for census tracts in which most buildings, demand and business establishments are subject to competition, and it meets the Commission’s criteria relating to geographic granularity and administrability.

A. The Competitive Market Test Proposed In The IRW White Paper Accurately Identifies Census Tracts Where Most Buildings and Demand Can Be Served By Multiple Providers Of BDS.

Accuracy of the Proxy. First, Drs. Israel, Rubinfeld, and Woroch demonstrate, using the 2013 dataset and other data collected by the Commission, that most buildings and demand in census tracts that pass the proposed Competitive Market Test can be served by multiple competitors, and that the proposed test thus reliably identifies competitive areas. Drs. Israel, Rubinfeld, and Woroch identified all of the specific census tracts that would pass the proposed Competitive Market Test, and used the 2013 data collected by the Commission, supplemented by national broadband data to identify the areas served by cable companies using HFC facilities, to

¹⁰⁹ *Id.* ¶¶ 292-95.

¹¹⁰ IRW Second White Paper at 27.

compute the percentage of buildings and demand in those census tracts that could be served by competing providers of BDS.

This analysis shows that more than 90% of buildings served by ILECs in the census tracts that pass the proposed test are within 2,000 feet of another provider's facilities, which is well within the Commission's finding that facilities-based competitors affect prices up to a half mile away.¹¹¹ The IRW Second White Paper analysis also confirms that these competitive buildings account for more than 90% of ILEC bandwidth and connections in those census tracts.¹¹² It also confirms that more than 95% of *all business establishments* in the census tracts that pass the proposed test are in census blocks with at least one other competitive provider in addition to the ILEC.¹¹³

Given that virtually all ILEC buildings and demand contained in census tracts that pass the proposed Competitive Market Test are within close proximity to another provider's network, it follows that *all* BDS services, including sub-50 Mbps BDS, are subject to competition in those census tracts. But to be sure that the sub-50 Mbps BDS are covered, the IRW Second White Paper separately analyzed competition for sub-50 Mbps BDS in the census tracts that pass the proposed test. This analysis shows that more than 90% of the buildings where ILECs have sub-50 Mbps connections are within 2,000 feet of at least one other provider's facilities. These data further show that more than 90% of ILEC sub-50 Mbps demand (*i.e.*, bandwidth) is located in buildings within at least one other provider within 2,000 feet. In short, the proposed Competitive

¹¹¹ See IRW Second White Paper at 28-31 & Tables 1-2.

¹¹² See *id.*

¹¹³ See *id.*

Market Test would capture census tracts in which virtually all sub-50 Mbps services being provided by ILECs are subject to competition from other providers.¹¹⁴

It is important to recognize that the proposed Competitive Market Test and the corresponding “validation” analyses presented in the IRW Second White Paper dramatically understate the true extent of competition in those census tracts. These analyses are based on the Commission’s 2013 data, which fails to account for the dramatic expansion in competitive facilities coverage that has occurred since then.¹¹⁵ The results reported above also do not account for competition from UNE-based providers.¹¹⁶

Geographic Granularity. The Commission currently regulates BDS at the MSA-level. MSAs are large geographic areas. There are about 381 MSAs in the U.S. The *Notice* raises concerns that MSAs are large and geographically diverse in the sense of having some areas with competitive BDS deployment and other areas without such deployment. The *Notice* thus raises concerns that de-regulation on an MSA-wide basis is over-inclusive in that it results in de-regulation in areas within MSAs that are not in fact subject to competition.

The proposed Competitive Market Test based on census tracts addresses these concerns. As the *Notice* recognizes, census tracts are much smaller geographic areas compared to MSAs, with the median census tract being only 1.5 miles across.¹¹⁷ Indeed, there are about 74,000 census tracts in the U.S. (compared to only about 381 MSAs).¹¹⁸ Most importantly, however, as shown above, the IRW Second White Paper shows that the census tracts that pass the proposed

¹¹⁴ *See id.*

¹¹⁵ *See id.* at 30-31.

¹¹⁶ *See id.*

¹¹⁷ *Id.* ¶ 213.

¹¹⁸ *See* IRW Second White Paper at 31-32.

Competitive Market Test are uniformly competitive, with more than 90% of buildings and bandwidth subject to competition from at least two providers. Thus, the concerns raised by the Commission about “over-inclusiveness” in MSAs, do not exist for census tracts.

The *Notice* correctly recognizes that attempts to regulate at even more geographically granular levels, such as the census block or building level would not be administratively practical.¹¹⁹ First, regulation at such granular levels would inevitably lead to a patchwork of differing regulations from census block to census block (or from building-to-building). Simply tracking which regulations apply in which census block would be an administrative nightmare for both regulators and providers – there are *millions* of census blocks, and tens of millions of buildings. Moreover, regulatory requirements that vary at such granular levels create enormous challenges to both providers and their customers when negotiating prices terms and conditions. For these reasons, adopting a competitive market test based on census tracts would represent a more appropriate compromise.

That is not to say that adopting a new regulatory regime at the census tract level would not impose significant costs or take significant time to implement, only that it would be less burdensome and costly than more geographically granular approaches. Even as such, the transition to a census-tract-based regulatory regime would still be very costly and time consuming to implement. Among other things, it would require providers to alter their systems to enable them to track and bill services among thousands of census tracts. AT&T estimates that revising its systems to track and bill for services at the census tract level would take approximately 18-24 months and divert tens of millions of dollars and the attention and expertise of many employees to making such revisions – capital and resources that would otherwise be

¹¹⁹ *Notice* ¶ 289.

available to make additional investments in the development and deployment of new services, technologies, and capabilities to meet the demands of customers. In addition, regulating services at the census tract level would require providers and customers to alter their contracting practices to ensure that contracts reflect regulatory differences at the much more geographically granular census tract level. For these reasons, the Commission should assess whether the benefits of establishing a new regulatory framework for these declining legacy services makes any sense at all. AT&T submits it does not, but to the extent the Commission chooses to regulate geographic areas smaller than MSAs, census tracts are a far more reasonable compromise than even smaller geographic areas.

Administrability. The proposed test would be workable. The Commission could use the 2013 data, supplemented with data for cable company HFC facilities, to determine which census tracts satisfy this test. Going forward, the Commission need only collect information from industry participants that identifies the location of their facilities in relation to census tracts.¹²⁰ This approach would also promote regulatory predictability by minimizing the number of variables and other issues that could lead to disputes and litigation about which locations meet the Competitive Market Test, and make resolution of disputes about whether a census tract satisfies the criteria easy to resolve.

B. The Commission Should Not Adopt The Product Market Definition For BDS Proposed In The *Notice*, Nor Should The Commission Evaluate Competition Based On Customer Classes.

The *Notice* raises two additional issues related to the Competitive Market Test: (1) how to define the “product market” for BDS for purposes of the test and (2) whether the test should account for different “classes” of customers.

¹²⁰ See IRW Second White Paper at 32.

1. The BDS Product Market.

The Competitive Market Test proposed in the IRW Second White Paper correctly recognizes that all facilities capable of providing broadband services to businesses should be included when assessing competition in the BDS marketplace. These facilities include copper, fiber, HFC, and fixed wireless facilities. The *Notice* also acknowledges that these facilities should be included when assessing competition for BDS.

The *Notice*, however, incorrectly proposes to count facilities only when they are used to provide business services that include certain levels of performance commitments. Specifically, the *Notice* proposes to define BDS as a service that “transports data between two or more designated points at a rate of at least 1.5 Mbps in both directions (upstream/downstream) with prescribed performance requirements that typically include bandwidth, reliability, latency, jitter, and/or packet loss.”¹²¹ The *Notice* states that this definition “does not include ‘best effort’ services, *e.g.*, mass market BIAS such as DSL and cable modem broadband access.”¹²² The *Notice* seeks comment on this definition.

To begin with, this definition is too vague to provide any predictability as to what facilities will be counted, and thus leaves providers in limbo as to whether the Commission might deem a particular area competitive. For example, it is unclear from the test which combination of performance metrics must be offered, and at what levels (*e.g.*, 99.99%, 99.00%, 95%). Providers thus have no way to determine *a priori* whether services they are developing will be subject to BDS regulation.

Moreover, there is no legitimate reason for the Commission to draw arbitrary lines between these different broadband services offered to businesses. As Dr. Israel, Rubinfeld, and

¹²¹ *Notice* ¶ 279 (internal quotations omitted).

¹²² *Id.*

Woroch have demonstrated, business customers choose the best combination of price and performance commitments that meet their needs, and providers compete for those customers by fine tuning the combination of price and performance metrics they offer.¹²³ There is no reason to assume that services reflecting different tradeoffs among those parameters are not substitutable, particularly when the underlying facilities are capable of offering all of the performance commitments. To the contrary, if two providers have deployed fiber facilities in an area, but have chosen to use those facilities to offer business services with different combinations of price and performance commitments, these providers are clearly competing. And, if one provider is more successful at winning customers, the other provider can easily revise its offering using its existing fiber facilities. There is no legitimate basis for the Commission to count some facilities, but not other facilities, based on the price and performance decisions made by the providers offering business services over those facilities when the facilities are capable of accommodating a variety of service parameters.¹²⁴

In particular, there is no basis for excluding “best efforts” services offered by cable companies over their HFC facilities in the definition of BDS.¹²⁵ Preliminarily, as the *Notice* acknowledges, cable companies use their HFC facilities, not only to offer best efforts Internet services, but also to offer Ethernet services that can and generally do include high performance commitments. Accordingly, even if the Commission were to find that “best efforts” services do not compete with the business services offered by ILECs and others over copper, fiber and fixed

¹²³ See IRW Second White Paper at 32-37.

¹²⁴ *Id.* Any attempt to draw those lines also could have perverse effects in the marketplace. By defining BDS with reference to performance parameters, the Commission would create incentives for providers to offer services with lower performance commitments in order to avoid BDS regulation of the prices and terms under which the services can be offered. The result could be less investment, less competition, and lower quality services.

¹²⁵ See *id.* at 34-37.

wireless facilities, the Commission still would have to include HFC facilities in its competitive analysis because those facilities are also used to provide Ethernet services. In economist terms, the two services are part of the same market because of the high elasticity of supply between them.

But even beyond this consideration, “best efforts” services offered by cable companies must be included within the definition of BDS. Such services typically offer speeds of 100 Mbps or more, which *far* surpasses the speeds available from legacy DS1 and DS3 services. And these higher speeds are often available at prices below those of legacy DS1 and DS3 services. As such, many customers view the higher speed and lower price as a justifiable trade-off for lower performance commitments. As explained by Professor Rysman: “some customers may view best-efforts broadband services as a viable alternative” to services that include performance commitments.¹²⁶

No equivocation is necessary on that point, as the record confirms that customers frequently do choose the faster and lower priced cable best efforts services over legacy DS1 and DS3 services, and that both ILECs and CLECs have lost a significant number of lower-bandwidth customers to cable best efforts services. AT&T demonstrated that, for the thirteen month period from November 2014 through November 2015, a very substantial portion of AT&T’s competitive losses were to cable companies and a significant portion of those losses were to best efforts cable services.¹²⁷ And CenturyLink reports that it “competes against all major cable companies, including but not limited to Comcast, Cox, Time Warner Cable, Charter,

¹²⁶ Rysman White Paper at 218. *See also* IRW Second White Paper at 34-27.

¹²⁷ Reply Comments of AT&T Inc., *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593, at 26-27 (filed Feb. 19, 2016).

and Brighthouse,” including against these cable companies’ “best efforts services” offerings.¹²⁸ CLECs are feeling the competitive heat as well. Hence, XO’s Director of Product Analytics admits that XO is “regularly competing” against cable companies for small and medium sized businesses, that it “loses” small and medium-sized customers “to [cable] companies offering Best Efforts Internet,” and that it has developed “products to this group of customers.”¹²⁹ And, Windstream’s website advertises its “Ethernet Internet” service (with a 99.99% uptime guarantee) as a substitute for best efforts cable.¹³⁰ TDS has likewise indicated that the vast majority of customers purchase lower-bandwidth services from TDS and that these customers have been “downgrading to best efforts broadband internet access services for cost savings.”¹³¹

AT&T and other ILECs have also demonstrated that they are now significant purchasers of cable company best efforts services as inputs to the data services they sell to retail customers. AT&T for example, has explained that it currently has contracts with **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED] **[END HIGHLY CONFIDENTIAL]** for the purchase of HFC-based “services outside of AT&T’s ILEC footprint,” and that it has certified these services for use as inputs to AT&T’s flagship MIS, VPN and backhaul services.¹³² Similarly, CenturyLink has demonstrated that “as a buyer of access,

¹²⁸ Reply Comments of CenturyLink, *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593, at 9-10 (filed Feb. 19, 2016) (“CenturyLink Reply”).

¹²⁹ Declaration of James A. Anderson ¶ 33 attached to Comments of XO Communications, LLC, *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (filed Jan. 27, 2016).

¹³⁰ See Windstream “Ethernet Internet,” <http://www.windstreambusiness.com/products/enterprise-network-services/dedicated-internet-services/ethernet-internet>.

¹³¹ Declaration of James Butman on Behalf of TDS Telecommunications Corp. ¶¶ 5, 15, attached to *Ex Parte* Letter from Thomas Jones (TDS) to Marlene H. Dortch (FCC), *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (filed Mar. 26, 2015).

¹³² Letter from Christopher T. Shenk (AT&T) to Marlene H. Dortch (FCC), WC Docket No. 05-25, RM-10593, at 7-8 (filed Mar. 21, 2016) (“AT&T March 21 Letter”).

CenturyLink has entered into various arrangements with cable companies, and has, over time, increased the volume of HFC-based services it acquires from them because of the value proposition they offer.”¹³³

Recent sales figures from cable companies also confirm their success in winning customers that would otherwise purchase DS1 and DS3 level services. For example, [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] increase for best efforts business broadband services from 2014-2015.¹³⁴ [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] from 2014 to 2015 increase in its BIA (its best efforts HFC service).¹³⁵ These substantial increases in sales can only come from customers that would otherwise have purchased services offered by ILECs and CLECs, such as DS1 and DS3 level services.

¹³³ CenturyLink Reply at 11-12. Further, cable companies themselves and industry analysts have emphasized the substitutability of cable best efforts broadband services for legacy DS1 and DS3 services. Comcast’s President has stated that “100 Mbps service is ideal for data-intensive businesses that need this kind of speed and want an alternative to slower, more expensive T1 lines.” Press Release, Comcast Corp., “Comcast Launches 100 Mbps High-Speed Internet Service for Business in the Twin Cities” (Sep. 8, 2009), <http://corporate.comcast.com/news-information/news-feed/comcast-launches-100-mbps-high-speed-internet-service-for-businesses-in-the-twin-cities>. See also, e.g., Press Release, Charter Comms., “Charter Business Customers Stay on the Leading Edge of Internet Speed with third Free Speed Increase for Commercial Customers” (Dec. 1, 2011), <https://newsroom.charter.com/press-releases/2011/charter-business-customers-stay-on-the-leading-edge-of-internet-speed-with-third-free-speed-increase-for-commercial-customers/> (“Charter Business Internet Essentials¹⁶, with downstream speeds of 16 megabits per second (Mbps) and upstream speeds of 2 Mbps, will increase to up to 20 Mbps downstream and 3 Mbps upstream . . . more than 13 times faster than T1.”).

¹³⁴ [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL]

¹³⁵ [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL]

The *Notice*'s reasons for excluding cable best efforts BDS are simply not valid. The *Notice* suggests that best efforts services' lower prices and lower performance commitments necessarily place them in a different market. But those conclusory assertions ignore the real world fact that customers frequently do choose best efforts services over higher priced services with performance commitments. The reasoning in the *Notice* establishes, at most, only that some customers are willing to pay more to get more and others prefer to pay less to get less, as is the case among products in almost every market. The key issue is whether customers in fact substitute best effort services for the more expensive options and, as explained above, the record shows that they do.

2. Customer Classes.

The *Notice* asks whether a different test should apply for different "classes" of customer on the grounds that "if supply to a first customer group cannot be readily extended to supply to a second, then supply to the first customer group may not place material competitive constraints on supply to the second."¹³⁶ The *Notice* does not propose any specific rules, but generally asks whether it should consider differences between large and small customers, multi-location customers, and whether customers use BDS for wholesale, mobile backhaul, or retail services. The Commission should reject all of these proposals.

First, the proposal is based on theoretical concerns that are not borne out by the facts. There is no record evidence of any systemic difference in the availability of competitive options for any particular "class" of customers. Rather, the record shows that providers deploy facilities in a particular area, and then compete for all customers in that area, regardless of whether the customer is a retailer, mobile provider, or wholesaler, and regardless of the size of the customer.

¹³⁶ *Notice* ¶ 199.

To be sure, there may be certain providers that specialize in certain types of BDS, but overall the evidence shows that providers generally can and do offer and sell services to all customer “classes.”

The *Notice* states that Commission Staff is “particularly interested in the extent that multisite customers may fall into” a separate “class” for the purpose of BDS regulation.¹³⁷ The *Notice* states that “multi-location customers are often provisioned by BDS providers that “have a broad regional footprint without significant gaps in coverage to serve large enterprises with multiple sites across given geographic regions.”¹³⁸ To the extent the Commission is thereby assuming that BDS providers with a “broad regional footprint” have market power in the provision of services to multi-location customers, such that those customers should be deemed a separate class, that assumption is flatly false.

First, this would be a solution in search of a problem as only a tiny portion of BDS customers are multisite customers. According to the 2013 data, businesses with fewer than 500 employees generally purchase BDS at only a single establishment,¹³⁹ and 99 percent of all firms have fewer than 500 employees. Moreover, more than 84 percent of establishments with BDS service have fewer than 500 employees. In other words, virtually all firms are single establishment customers, and those firms account for the vast majority of all establishments with BDS demand.

In any event, the notion that multisite customers are somehow lacking in competitive alternatives has it exactly backwards.¹⁴⁰ Multisite BDS customers are among the most desirable

¹³⁷ *Id.*

¹³⁸ *Id.* ¶¶ 199, 201.

¹³⁹ *See id.* ¶ 73, Table 1.

¹⁴⁰ *See* IRW Second White Paper at 38-39.

of all customers, and, as a result, they are *especially* sought out by BDS providers who compete vigorously for their business. And because they tend to be large volume customers, they are typically more aggressive in their requirements and during negotiations, and are able to command the best rates, terms and conditions. Further, because these customers tend to be larger and more sophisticated purchasers of BDS than other customers, they are especially well positioned to take full advantage of the intense rivalry that exists among BDS providers for their business. They typically purchase services using RFPs, negotiate bottom line prices, use different providers in different locations to get the best deal, and otherwise have substantial negotiating leverage. Far from representing a customer class in need of special regulatory protection, these customers are, if anything, in a class that warrants *less* protection.¹⁴¹

Not only is there is no need for the customer class distinctions suggested in the *Notice*, but any attempt to implement different regulations based on customer class would be an administrative nightmare that would lead to regulatory arbitrage, costly disputes, and reduced competition. For example, many BDS contracts often do not distinguish between ports used for “retail” and ports used for “wholesale.” If the Commission were to adopt rules that regulated customer class differently, that could mean that services sold by AT&T would be regulated differently depending on how the customer uses those circuits. It would be enormously costly for AT&T to develop systems that track how its customers use their services. Moreover, this approach would inevitably create opportunities for regulatory arbitrage that would lead to costly disputes, as purchasers attempt to designate purchases as being associated with the customer class that offers the most favorable rates, terms and conditions.

¹⁴¹ It is also important to recognize that for larger multisite customers, *no provider* – not even an ILEC – can offer facilities-based coverage for all locations. Rather, all BDS suppliers that seek to serve such customers most likely would need to do so using a combination of their own facilities and facilities leased from other BDS providers.

Attempting to classify businesses based on size – whether in terms of employees or some other measure – raises similar problems. Many purchasers of BDS are affiliates, subsidiaries or parent companies, which raises the question of how to compute the “size” of a customer. In some cases, the parent company may negotiate the purchase of BDS for its affiliates and subsidiaries, and in those cases the “size” of the company would likely be based on aggregate size of the parent, affiliates and subsidiaries. In other cases, a small subsidiary may independently purchase the service, in which case the size of the small subsidiary may be the relevant metric. Moreover, the size of a BDS customer – however measured – can increase or decrease, which raises the question as to whether the terms and conditions under which a customer purchases BDS must be changed when the customer grows or shrinks (or acquires or divests), which would impose additional costs and uncertainty on the industry. For these reasons, it is impossible to create a bright line rule, and there would be significant incentives for purchasers to attempt to qualify for whichever “size” is associated with the most favorable regulations, thus resulting in regulatory arbitrage, endless disputes, and more costly services.¹⁴²

C. Number of Competitors

The *Notice* asks whether two competitors are sufficient to ensure competitive results. The answer is yes. The Commission has previously determined that the presence of a single facilities-based competitor to an ILEC is sufficient to ensure competition because “the presence of facilities-based competition with significant sunk investment[s] make exclusionary behavior

¹⁴² Devising regulations based on the classes proposed in the *Notice* is also based on the false premise that customer needs of BDS necessarily correlate with the factors identified for categorizing customers by class, but that is not the case. For example, many technology customers with only a small number of employees purchase highly sophisticated, secure, high capacity, and reliable BDS. By contrast, many larger companies, in terms of employees, require lower bandwidth and less sophisticated suites of BDS. Implementing a system that provides smaller customers with regulated access for services would also distort the marketplace by giving smaller BDS purchasers a regulatory advantage over their larger competitors.

highly unlikely to succeed.”¹⁴³ The D.C. Circuit agreed with this reasoning. It explained that “the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed.”¹⁴⁴ The Justice Department has likewise determined in merger proceedings that no divestitures were required in buildings where, post merger, there would be one additional competitor at or nearby the building, because the likelihood of anticompetitive harm was “unlikely.”¹⁴⁵

Professors Israel, Rubinfeld, and Woroch further explain that two providers is sufficient to ensure competitive outcomes.¹⁴⁶ First, “there is a natural variation in the number of special access competitors connected to buildings of different sizes. Smaller buildings may support only one or two providers, while larger ones may support many competitors.”¹⁴⁷ Accordingly, “there is no basis for concluding that competition is less intense in smaller buildings with fewer connections by competitors.”¹⁴⁸ Indeed, “[e]ach competitor connected to a building has strong

¹⁴³ Fifth Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, 14 FCC Rcd. 14221, 14264, ¶ 80 (1999).

¹⁴⁴ *WorldCom*, 238 F.3d at 458-59.

¹⁴⁵ Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp., Application for Transfer of Control*, 22 FCC Rcd. 5662, 5682-83, ¶¶ 41-42 (2007) (discussing the consent decrees). See also AT&T March 21 Letter at 5.

¹⁴⁶ See Declaration of Mark Israel, Daniel Rubinfeld, and Glenn Woroch, *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, at 11-12 (Feb. 19, 2016) attached to Reply Comments of AT&T Inc., *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (Feb. 19, 2016).

¹⁴⁷ *Id.*

¹⁴⁸ *Id.*

incentives to make maximum use of its facilities, and, thus will compete vigorously to win customers in the building.”¹⁴⁹

Second, in the BDS marketplace, once BDS capacity has been deployed to a building, it can be upgraded to increase capacity at very low cost. For this reason, each competitor that serves a building will typically be able to serve all demand in the building. “Each competitor, therefore, will have substantial incentives to compete for all customers in a building. Thus, with even two providers connected to (or nearby) a building, customers within the building will generally enjoy the benefits of intense competition among providers attempting to generate additional returns on largely sunk investments.”¹⁵⁰

Third, “to the extent other competitors have deployed nearby fiber facilities, any attempt by competitors that are already connected to a building to charge above competitive prices will induce other competitors to compete for those customers and build their own connections to the building. As long as competitors have sunk facilities capable of competing for demand in the building, there is no legitimate basis for concluding that competition will be less with fewer competitors connected to a build.”¹⁵¹

IV. THE COMMISSION SHOULD NOT MODIFY THE X-FACTOR OR ADJUST THE CURRENT PRICE CAPS FOR LEGACY TDM BDS.

The Commission need not attempt to adopt a new, BDS-specific X-Factor or reset the caps for BDS for three fundamental sets of reasons: (1) the Commission has not justified the

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.* The results of the Rysman regressions – purporting to show slightly lower prices in areas where there are either three or four competitors compared to areas where there are two competitors – are not to the contrary. For the reasons described above, Professor Rysman’s regressions are unreliable and thus are not a legitimate basis from which to draw any conclusions about any issues in this proceeding, including the number of competitors needed to achieve competitive outcomes.

need for, or the methodology for calculating, any new BDS-specific X-Factor; (2) the best estimate of a forward-looking X-Factor based on publicly available data is 1.95 percent; and (3) there is no basis in the record for a one-time downward adjustment to the BDS-specific price cap.

A. There Is No Justification for a New BDS-Specific X-Factor.

At the most basic level, the Commission has not made a case that it either needs to, or can defensibly design, a BDS-specific X-Factor.

First, there is nothing in the record that would justify a finding that the rates produced by today’s price cap rules are unjust and unreasonable.¹⁵² The brief musings in the *Notice* as to why the current X-Factor might permit unjust and unreasonable rates are not to the contrary.¹⁵³ The Commission simply asserts, with no citation to the record, that price cap LECs have been consolidating TDM switches, placing soft-switches, increasing fiber deployments, and decreasing maintenance costs.¹⁵⁴ The Commission also suggests that the price cap LECs have experienced growth in output and therefore increasing economies of scale and reduced costs.¹⁵⁵ Based solely on these assertions, the Commission “believes” that productivity gains have

¹⁵² See, e.g., *Fed. Power Comm’n v. Conway Corp.*, 426 U.S. 271, 278 (1976) (“[T]here is no single cost-recovering rate, but a zone of reasonableness: Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint.” (quotation omitted)); *Montana-Dakota Util. Co. v. Nw. Pub. Serv. Co.*, 341 U.S. 246, 251 (“Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high.”).

¹⁵³ *Notice* ¶ 366.

¹⁵⁴ *Id.*

¹⁵⁵ *Id.* ¶ 365.

“significantly outpaced inflation” and that price cap LECs are “likely” charging unreasonably high rates for DS1s and DS3s.¹⁵⁶

Any reliance on these unsupported assertions as the basis for adopting a new X-Factor would be arbitrary, for at least two reasons. First, the X-Factor for the last decade was not zero – it was set equal to inflation. Accordingly, since 2005 the current X-Factor has resulted in an approximately 26 percent reduction in DS n prices over the last decade in real terms. The Commission has not even attempted to show that the cost reductions it claims, to the extent they occurred, resulted in productivity gains that are “significantly” in excess of those levels.¹⁵⁷ Indeed, the Commission’s claims in this regard are refuted by the analysis of its own consultant, Professor Rysman. Professor Rysman’s analysis was unable to conclude that DS3 pricing was in any way excessive, and at best it discerned a small 3.2 percent divergence in DS1 pricing. Given that GDP-PI incorporates national productivity gains, Professor Rysman’s analysis (even if it could be credited) is conclusive that DS n productivity has not exceeded national productivity in recent years.

Second, and equally important, the developments the Commission cites do not support its conclusion that price cap carriers are experiencing productivity gains in DS n services. For one thing, demand for DS n services has been in rapid decline in recent years, as price cap LECs retire their legacy TDM networks. Indeed, AT&T’s non-affiliate billed revenues for TDM-based DS1 services declined by more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END

¹⁵⁶ See also *id.* ¶ 401 (Commission’s analysis “suggests” that price cap carriers have achieved significant productivity gains and cost savings since the expiration of the CALLS Plan on June 30, 2005).

¹⁵⁷ *Cf. id.* ¶ 366.

HIGHLY CONFIDENTIAL] in the last two years,¹⁵⁸ and as a result AT&T is currently experiencing very low utilization on its legacy TDM switches. The accompanying loss of scale economies suggests that it is unlikely that price cap LECs have achieved productivity gains that are in excess of inflation. But beyond that, the Commission is mistaken with respect to the other factors it cites as evidence of large productivity gains. “Consolidation” of TDM switches serves largely to keep pace with declining demand rather than improve productivity. The “placement of softswitches” has almost nothing to do with legacy DSn services, and in fact, AT&T has replaced only a small number of its TDM switches with softswitches. And finally, the deployment of fiber infrastructure also mostly redounds to the benefit of other services, such as Ethernet or broadband Internet access services.

Equally important, as demand for DSn services continues to decline rapidly and carriers move toward retiring their legacy TDM facilities, there is no reasonable expectation that LECs will achieve meaningful productivity gains in providing these services in the future.¹⁵⁹ Indeed, price cap LECs are not only serving a rapidly declining customer base over legacy copper and other TDM facilities that are earmarked for retirement, but they are also having to maintain an MPLS network to facilitate interaction between those legacy facilities and modern services like Ethernet. The Commission’s stated policy goal is to encourage the deployment of broadband networks. Increasing the X-Factor to drive down DSn rates – which could only boost incentives for LECs to divert resources toward trying to achieve productivity gains for DSn services – would be directly contrary to that goal.

¹⁵⁸ Declaration of Paul Reid ¶ 4, attached to Brief of AT&T Inc. in Support of Its Direct Case, *Investigation of Certain Price Cap Local Exchange Carrier Business data Services Tariff Pricing Plans*, WC Docket No. 15-247 (Jan. 8, 2016).

¹⁵⁹ This is especially true given that, as explained above, after application of the Competitive Market Test, the price caps will apply only to the DSn services offered in the costliest and most sparsely populated areas, where productivity gains would be the hardest to achieve.

In that regard, the Commission is especially misguided in claiming that AT&T’s “public statements make clear that its productivity gains are significant and very likely exceed those for the general economy.”¹⁶⁰ The Commission quotes AT&T’s 10-K Annual Report as saying “[n]etwork costs decreased \$434 [million] primarily due to lower interconnect costs resulting from our ongoing network transition to more efficient Ethernet/IP-based technologies.”¹⁶¹ This AT&T statement has nothing to do with productivity gains AT&T may have achieved in the provision of DS1 and DS3 services. Rather, the statement appears in the section of the 10-K discussing the results for AT&T’s Consumer Mobility segment, and indicates that Consumer Mobility was able reduce its network costs by \$434 million primarily by reducing its “interconnect” costs. In other words, the Mobility unit is paying less money to third parties for interconnection because it continues to transition to more efficient Ethernet and IP-based technologies – a fact that, to the extent it is relevant at all, further confirms that legacy TDM services are not experiencing significant productivity gains.

B. The Commission’s Proposals For A New X-Factor To Be Applied Prospectively Have Significant Deficiencies.

The Commission seeks comment on how to devise a new, productivity-focused X-Factor that would apply prospectively in the price cap formula. As explained below, the best available method of measuring the X-Factor based on publicly available data suggests that it should be no more than 1.95 percent.

The Commission seeks comment on three possible methodologies for calculating a “productivity-based X-Factor” that use “projections of productivity gains, rather than actual

¹⁶⁰ Notice ¶ 401 & n.908.

¹⁶¹ *Id.* ¶ 80 n.207 (quoting AT&T Inc., Annual Report (Form 10-K) (Feb. 18, 2016)) (alteration in original).

values, based on historical trends.”¹⁶² Only one of its proposed methodologies (with minor adjustments) is at all appropriate, because it is the only one that relies on both well-accepted economic theory and publicly available data. In contrast, the other methods would be egregiously inappropriate.

The only appropriate methodology of the three proposed by the Commission relies on the U.S. Bureau of Labor Statistics’ (“BLS”) Capital, Labor, Energy, Materials, and Services data (“KLEMS”). Indeed, this is the only one of the Commission’s three data sources that is actually intended to be a measure of total factor productivity.¹⁶³ As Drs. Meitzen and Schoech explain, BLS’s data would produce an X-Factor of 1.95 percent, if the Commission were to rely on data from 2005-2013.¹⁶⁴ Although the Commission could adopt this X-Factor, an X-Factor of that magnitude would likely not be sufficiently different from inflation to necessitate a rule change – especially considering that this X-Factor would apply only to a small set of services that will be obsolete in a few years.

¹⁶² *Id.* ¶ 376.

¹⁶³ *See id.* ¶ 378 (“The KLEMS data used in our calculations are publicly available, annual industry-level data on industry-level measures of input prices and total factor productivity (TFP) for the telecommunications and broadcasting industries.”); *see also* Christensen Paper at 5 (“The KLEMS database is developed using rigorous total factor productivity principles and is a valid source of measuring total factor productivity and input price trends for various industries.”).

¹⁶⁴ Christensen Paper at 7-9 & Table 1. Drs. Meitzen and Schoech explain that in determining “the appropriate forward-looking X-factor from historical data, it is important to balance the need for stability in the X-factor number with basing the results on recent productivity and market trends.” *Id.* at 9. “Using a shorter period may be better at capturing recent trends, but the relatively large year-to-year variations in productivity may lead to an unstable X-factor projection. On the other hand, using a long period would produce a more stable series but includes relatively stale data. In our opinion, using the period 2005-2013 in setting the X-factor appropriately balances these two considerations.” *Id.* Dr. Meitzen and Schoech’s calculations involve minor corrections to the Commission’s BLS-derived calculations, because the Commission used a method of aggregating the KLEMS data input measures that “is not conventional and is not consistent with the indexing methods used by the BLS.” Christensen Paper at 8; *cf. Notice* ¶ 407, Table 7.

But even this BLS-derived X-Factor likely overstates expected productivity gains for the DS_n services to which it would apply. BLS publishes only an industry-wide measure encompassing productivity gains in the broadcasting and telecommunications industries. Because telecommunications represents an overwhelming share of the combined telecommunications plus broadcasting industries, by itself this does not present a significant problem because nearly all of the measured productivity growth will be due to telecommunications advances.¹⁶⁵ Most of the telecommunications productivity gains captured in the BLS measure, however, are likely attributable to productivity gains in *other* telecommunications services that are the focus of far greater investment and technological dynamism than legacy DS_n services, including wireless services, broadband Ethernet services, and cable and wireline Internet access services. Thus the industry-wide BLS measure likely overstates productivity gains for the small subset of TDM-based DS_n services.

The Commission's second proposed methodology would rely on data from its Connect America Cost model ("CACM").¹⁶⁶ The CACM data, which is used primarily for universal service purposes, consist solely of forward-looking economic cost estimates of several cost categories for a mass market residential and small business broadband network that also provides voice services. As demonstrated by Drs. Meitzen and Schoech, the CACM models simply cannot provide reliable estimates of ILEC productivity gains for legacy TDM-based DS_n services over time.¹⁶⁷

¹⁶⁵ Christensen Paper at 5.

¹⁶⁶ *Notice* ¶¶ 377, 379. The *Notice* leaves open whether the Commission might use the CACM data in addition to or in lieu of the BLS data.

¹⁶⁷ Christensen Paper at 9-13.

REDACTED – FOR PUBLIC INSPECTION

To begin with, the purpose of these data is to estimate *relative* costs of best-effort broadband networks uniformly and instantaneously deployed in rural and non-rural areas at a point in time. The CACM was not designed to accurately capture the *actual* cost of any network that provides DSn BDS, nor to estimate historical changes in network costs.

Moreover, the CACM does not contain any reliable historical data that could be used to produce historical cost change estimates. The Commission has in the past admitted that attempts to fill in historical price changes are unreliable due to the lack of data regarding the various cost categories (*e.g.*, fiber, poles, conduit, drop, optical network terminals, fiber pedestals, and splitters). As the Commission itself has previously explained, “[w]e do not have good data sources for the history of price changes for [these] inputs.”¹⁶⁸

Even if the CACM could be used to measure cost changes over time, it cannot be used to measure cost changes for legacy TDM-based DSn services. The CACM is designed to measure forward-looking costs of a residential or small business “best efforts” broadband network that also provides voice services. Thus, its costs and trends would bear little relationship to the costs and costs trends of a legacy TDM network that provides special access services with guaranteed performance standards and customized configurations to particular customer locations. As the Commission itself contends elsewhere in the *Notice*, legacy TDM-based DSn service “tends to cost substantially more than ‘best efforts’ services and are offered to businesses, non-profits, and government institutions that need to support mission critical applications and have greater

¹⁶⁸ Federal Communications Commission, *Peer Review of Connect America Phase II Cost Model, FCC Response to Professor Christiaan Hogendorn* 11, https://apps.fcc.gov/edocs_public/attachmatch/DOC-322385A1.pdf.

demands for symmetrical bandwidth, increased reliability, security, and service to more than one location.”¹⁶⁹

Moreover, the CACM models an *all fiber* network, including the last mile portion of the network. By contrast, legacy TDM-based networks are fiber-copper networks, with a large portion of last mile facilities comprised of legacy copper facilities. The Commission has no legitimate basis for assuming that legacy (and soon to be retired) copper networks share the same evolution of efficiencies as next-generation fiber-based services.¹⁷⁰ Finally, the CACM makes no attempt to estimate the cost of any of the middle-mile or interoffice fiber needed to supply BDS – as well as any of the BDS-specific transmission or routing equipment or any of the service ordering, provisioning, billing or maintenance systems employed by BDS. Indeed, the network designed by CACM is for mass market services – which differs fundamentally from a network and cost structure for BDS which are purpose-designed circuits.

For purposes of the *Notice*, Commission Staff appears to have modified the CACM and introduced various forms of historical data in an attempt to produce historical cost changes, and hence efficiency estimates. According to the *Notice*, the Commission relied on “cost models and industry financial accounts” to determine “the key cost components of business data services supply, estimate[] their shares, and estimate[] changes in the input prices of each key

¹⁶⁹ *Notice* ¶ 13.

¹⁷⁰ The Commission dismisses this concern in a single sentence, with no explanation or any citation to the record. *Id.* ¶ 409 (“[I]t is essentially a model of the costs of an incumbent LEC supply, but with a focus on residential rather than business data services. Despite this, there are no reasons to think that either (1) the underlying cost categories of the CACM or (2) the rates of change in input prices of these cost categories would be significantly different for business data services than for residential data services.”). *See also* Christensen Paper at 11 (“[i]n fact, the actual provision of special access is much more labor intensive because of the customized, customer-specific nature of these services – which is in marked contrast to the uniform engineering assumptions of mass market services”).

component.”¹⁷¹ But the Commission provides no details about how it conducted these calculations, and, as it previously recognized, no reliable sources of information exist that could be used to obtain accurate historical cost estimates using the CACM.¹⁷² But in all events, any such efforts would be pointless because the CACM does not model costs for legacy TDM-based networks. At the end of the day, any X-Factor based on the CACM would be inherently arbitrary.

The Commission’s third proposed methodology would rely on data from the CACM “in combination with cost data that TDS submitted in this proceeding.”¹⁷³ This “combination,” however, would suffer from even more flaws than the second proposed methodology. Adding the TDS data would not address or eliminate any of the fundamental shortcomings with the CACM data. And the TDS data itself are of little value because they are merely proprietary, unvalidated data from a single competitor that is seeking regulation.¹⁷⁴

Finally, there is no conceivable justification today for a “Consumer Productivity Dividend.”¹⁷⁵ The Commission first adopted the Consumer Productivity Dividend during the initial transition from rate-of-return to price cap regulation, on the theory that incentive

¹⁷¹ *Id.* ¶ 408.

¹⁷² Christensen Paper at 11-12 (“[i]n our view, this process provides little comfort or assurance that these hypothesized input price series, or their growth, bear any relationship to actual input prices, particularly for the legacy networks that provide the majority of BDS; if anything, it indicates that another level of unverifiable estimates are layered on top of the hypothetical proxy model input prices this approach begins with”).

¹⁷³ *Notice* ¶ 377. Notably, the data TDS proffers are from its ILEC subsidiary, which operates generally small rural rate-of-return regulated LECs.

¹⁷⁴ Christensen Paper at 13. In the same vein, adding TFP data from the San Francisco Federal Reserve Board would not be useful because these data purports only to measure economy-wide TFP. Such data are certainly inferior to the KLEMS data that measure telecommunications and broadcasting TFP in addition to national TFP. *See id.* at 6-7.

¹⁷⁵ *See Notice* ¶ 382.

regulation would spur the price cap LECs to achieve a higher level of productivity in the future that would not have been reflected in the historical data, which at the time came solely from the rate-of-return era. This dividend was maintained during the Commission’s first review of its LEC price cap plan because this review continued to dismantle the inefficient incentives of legacy rate-of-return regulation by eliminating earnings sharing. But now after two and a half decades of incentive regulation, there is no longer any basis for such a “catch-up” factor; to the contrary, as price cap carriers move to *retire* the legacy TDM networks used to provide DS_n services, it is quite possible that DS_n productivity growth rates will decline in future years.¹⁷⁶ The Commission’s goal should be to encourage investment in broadband alternatives; it should not adopt measures like the “Consumer Productivity Dividend” which, by its nature, would represent an attempt to goad carriers to achieve extraordinary productivity gains above historical norms in these legacy TDM networks that are being retired.¹⁷⁷

C. The Commission’s Proposed “Baseline Price Cap Level Adjustment” Would Also Be Unlawful.

The Commission also seeks comment on whether it should implement a one-time reduction in the BDS-specific price caps to reflect productivity gains price cap LECs allegedly may have achieved in excess of inflation since 2005, the last year of the CALLS Plan.¹⁷⁸ There is no basis in the record for such an adjustment, for several reasons.

¹⁷⁶ Indeed, the D.C. Circuit found the Commission’s attempt to retain the Consumer Productivity Dividend in 1997 to be arbitrary, almost two decades ago. *United States Tel. Ass’n v. FCC*, 188 F.3d 521, 527 (D.C. Cir. 1999) (“*USTA*”).

¹⁷⁷ Christensen Paper at 4 (“[g]iven that the current proposed price cap plan for BDS represents neither a transition to a more incentivizing regulatory regime nor a relaxing of a regulatory constraint, the addition of a CPD in this case, in our opinion, is not appropriate”).

¹⁷⁸ See Notice ¶¶ 401-15

First, the Commission’s own data confirm that no downward adjustment would be appropriate. The BLS data – which is the only one of the Commission’s three methodologies that actually attempts to measure total factor productivity – produces an X-Factor over the 2005-2013 period that is almost exactly equal to the inflation factor and thus would require a less than 0.5 percent adjustment to the present cap.¹⁷⁹ That is not an adjustment worth making. Moreover, even that calculation overstates the price cap LECs’ productivity gains for DSn services. As explained above, the BLS data measure productivity gains for the entire communications industry, and thus most of the gains captured in those figures are attributable to *other* services, like broadband and wireless services, that have been the focus of the industry’s investment and technological advances.

The Rysman analysis is not to the contrary. As noted, that analysis is unreliable both because of incomplete and unreliable data inputs and because it lacks the data necessary to distinguish correlation from causation. But even assuming *arguendo* that Professor Rysman’s results are accurate, they do not support a one-time baseline price cap level adjustment. At most, those regression analyses find that the price cap LECs’ rates in competitive areas are only slightly below those in “non-competitive” areas (about three percent for DS1 services). Given that price cap LECs would have had no choice but to pass productivity gains on to customers in the areas Professor Rysman is willing to deem competitive, his results confirm that price cap LECs could not have achieved significant productivity gains over inflation since 2005 that would justify a one-time adjustment.

As explained above, it would be patently arbitrary to use either of the Commission’s other two proposed methodologies to estimate historical productivity. Using such methodologies

¹⁷⁹ See *id.* ¶ 407, Table 7; Christensen Paper at 8, Table 1.

to estimate a *reduction* of the caps from 2005 levels, however, would be unlawful for the additional reason that the Commission cannot rationally treat the price cap levels of 2005 as representing an accurate measure of the productivity gains price cap LECs had achieved as of that date. To the contrary, the price cap levels of 2005 were the product of almost a decade of unlawfully high X-Factors that federal courts of appeals found twice to be arbitrary and which likely had forced price caps to artificially low levels.¹⁸⁰ Indeed, from 2000-2005, the X-Factor was not even intended to be a measure of productivity, but rather was simply a mechanism to drive rates to the agreed-upon levels in the context of the much larger CALLS Plan agreement, which represented an industry-wide settlement of a large range of outstanding issues and disputes.¹⁸¹ Thus, in addition to the other flaws of relying on CACM-related measures to impose a one-time, downward reduction in the caps, the Commission could not impose any such adjustment without first backing out the unlawfully high 6.5 percent X-Factors that applied during most of the 1997-2005 period.¹⁸²

V. THE COMMISSION SHOULD REJECT ITS ADDITIONAL PROPOSALS FOR REGULATION OF “NON-COMPETITIVE” SERVICES.

The Commission proposes various additional regulations that may apply in areas the Competitive Market Test deems “non-competitive,” including rules relating to (1) “wholesale”

¹⁸⁰ *USTA*, 188 F.3d at 526 (finding that the Commission made “irrational” choices both in establishing the range of reasonableness and in selecting a value within that range); *Texas Office of Public Util. Counsel v. FCC*, 265 F.3d 313, 328-29 (5th Cir. 2001).

¹⁸¹ Access Charge Reform, *Sixth Report and Order in CC Docket Nos. 92-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45*, 15 FCC Rcd. 12962, 12978, ¶ 40 (2000) (noting that the CALLS Plan “treats the X-Factor not as a productivity estimate but as a method to reduce rates to certain levels”); *see also id.* ¶ 41, n.51 (noting that if the rate of inflation rises above current levels, LEC rates would be forced down in real terms even more quickly).

¹⁸² *Cf.* Christensen Paper at 8-9, Table 1 (actual, realized total factor productivity gains based on BLS data during the period 1997 through 2003 averaged 2.02 percent).

services, (2) terms and conditions, and (3) a kind of “faux” detariffing. The Commission should reject each of these proposals.

A. The CLEC Proposal To Add An Additional New Layer of Regulation For “Wholesale” Purchases Is Unnecessary And Would Impede Investment And Slow The Transition To IP-Based Services.

Certain CLECs purport to have identified isolated instances in which ILEC wholesale BDS rates are higher than ILEC retail BDS rates, and ask the Commission to adopt sweeping regulations that would require wholesale BDS prices to be set at levels below retail levels.¹⁸³ The Commission should reject these requests. First, claims that wholesale rates are in a few isolated cases higher than retail rates are false. More importantly, a handful of anecdotes do not provide any basis for national rules; those claims can and should be handled through the section 208 process. And in all events, such claims provide no basis for a rule mandating that wholesale rates be *lower* than retail rates. Any such rule would be unlawful in numerous respects.

As a preliminary matter, the Commission could not lawfully mandate new wholesale BDS rates. The Communications Act establishes a regime of carrier-initiated rates.¹⁸⁴ Once such rates take effect, the Commission may order a carrier to change the rates it offers only after the Commission has (1) made definitive findings that the carrier’s existing charge or practice “is or will be in violation of any provisions of [the Act]” and (2) determined “what will be the just and reasonable” charge or practice “to be thereafter followed.”¹⁸⁵ There is no record here on

¹⁸³ Notice ¶¶ 441-42.

¹⁸⁴ *AT&T Co. v. FCC*, 487 F.2d 865, 871 (2d Cir. 1973); *Am. Broadcasting Co., Inc. v. FCC*, 643 F.2d 818, 822 (D.C. Cir. 1980).

¹⁸⁵ 47 U.S.C. § 205; *see also AT&T Co.*, 487 F.2d at 874 (express Commission findings that the carrier-initiated rate is unjust and unreasonable and the prescribed rate is just and reasonable “are essential to any exercise by the Commission of its authority” to prescribe rates); *Sw. Bell Corp. v. FCC*, 43 F.3d 1515, 1519 (D.C. Cir. 1995). Those principles should apply with even greater force to any Commission attempt to dictate what rate a carrier may charge for services that have been detariffed.

which the Commission could make such findings with respect to each wholesale rate. There is accordingly no basis upon which the Commission could mandate that wholesale rates be categorically reduced to reflect a wholesale discount.

Indeed, the record contains no reliable evidence that rates for *any* service are above competitive levels. Professor Rysman’s analysis of incumbent LEC DS1 and DS3 rates is concededly problematic and proves, *at worst*, that such rates are only nominally higher than competitive market rates in certain areas. And there is no evidence at all that Ethernet rates of any bandwidth are unreasonable. Accordingly, the Commission could not possibly make the requisite statutory findings to order reductions in BDS rates to accommodate wholesale discounts. Any such requirement would necessarily force rates *below* competitive levels.

The Commission seeks comment on whether it could nonetheless mandate wholesale discounts under Sections 201 and 202.¹⁸⁶ It could not. The Commission has never held that Section 201 or 202 gives it the authority to mandate wholesale discounts for generally available services. To the contrary, those provisions have always been deemed to prohibit use restrictions for interstate services. Use restrictions categorically deny certain customers the same rates, terms and conditions available to others and consequently have long been deemed unreasonably discriminatory.¹⁸⁷ And so it would be with wholesale discounts insofar as such discounts would

¹⁸⁶ Notice ¶ 443.

¹⁸⁷ See, e.g., Report and Order, *Amendment of Sections 64.702 of the Commission’s Rules and Regulations (Third Computer Inquiry); Policy Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Thereof*, 104 F.C.C. 2d 958, 1042, ¶ 165 (1986) (prohibiting carriers from “restrict[ing] the availability of CEI [comparably efficient interconnection] to any particular class of customer or enhanced service competitor” because such restrictions are “anticompetitive discrimination”); Memorandum Opinion and Order on Reconsideration, *Amendment of Sections 64.702 of the Commission’s Rules and Regulations (Third Computer Inquiry); and Policy and Rules Concerning Rates for Competitive Common Carrier Service and Facilities Authorizations Thereof*, 2 FCC Rcd. 3035, 3051, ¶ 109 (1987) (noting Commission’s “longstanding policies against tariff restrictions on service availability

preclude retail customers from obtaining the same rates as wholesale customers for the exact same services.

The Commission also asks whether Section 251(c)(4)¹⁸⁸ could provide it with legal authority to regulate wholesale BDS rates. The answer is a firm no. Section 251(c)(4) sets forth a resale standard to be applied in the context of competition for mass market local retail telephone service, and thus would be a singularly inappropriate vehicle for regulating individually negotiated BDS rates. The Commission has long held that Section 251(c)(4) does not apply, and was not meant to apply, to interstate access services, which have been largely provided on a wholesale basis.¹⁸⁹ And it has also recognized that it would make no sense to apply section 251(c)(4) to such services insofar as that provision limits discounts to avoided costs, consisting mostly of marketing and other retailing costs that simply do not exist in the context of BDS.¹⁹⁰

Moreover, any attempt to apply Section 251(c)(4) to BDS would hopelessly complicate regulation of these services, because Sections 251 and 252 mandate that such arrangements be negotiated in interconnection agreements that are adjudicated and enforced by state commissions. Indeed, under Section 252(d)(3), each state commission would set its *own* discount, not the Commission. Such a scheme would balkanize all wholesale BDS arrangements

based on user or service classification”); Memorandum Opinion and Order, *MCI v. AT&T*, 94 F.C.C. 2d 360, 391-92, ¶¶ 97-100 (1981) (finding that use restriction violated Sections 201 and 202). The only statutory exception is the one *expressly* provided in Sections 251 and 252, which for the reasons explained below do not apply here.

¹⁸⁸ 47 U.S.C. § 251(c)(4).

¹⁸⁹ See First Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd. 15499, 15935, ¶ 874 (1996).

¹⁹⁰ See *id.* (“[B]ecause access services are designed for, and sold to, IXC’s as an input component to the IXC’s own retail services, LEC’s would not avoid any ‘retail’ costs when offering these services at ‘wholesale’ to those same IXC’s.”).

into state-by-state agreements and transfer much of the authority to regulate these quintessentially interstate services to the state commissions.

Further, the Commission has indicated that all firms should be subject to the same regulatory requirements for BDS. But Section 251(c)(4) applies only to ILECs,¹⁹¹ and therefore could not provide the Commission with authority to regulate wholesale BDS rates for all carriers. In short, there is no statutory, policy, or practical rationale for applying Section 251(c)(4) to BDS.

Even if there were a statutory basis for mandating wholesale discounts on BDS, there is no valid policy reason to do so. CLECs could not possibly claim that BDS competition depends on such discounts because without them they already have won more than half of all BDS revenues. And while they loosely toss around the term “price squeeze,” these claims fall flat because there is no evidence in the record that any provider of Ethernet services has the requisite market power to effect a price squeeze. To the contrary, Professor Rysman found no evidence of market power in his analysis of above 45 Mbps services, and Drs. Israel, Rubinfeld and Woroch, conducting the same test used by Professor Rysman for sub-45 Mbps services, found no evidence of ILEC market power for those services either. These findings are not surprising because the Ethernet marketplace is structurally competitive. There are nine competitors with market shares between 4 percent and 18 percent (two are ILECs, four are CLECs (counting Verizon), and three are cable companies), and there are dozens more competitors with a cumulative market share of more than 18.5 percent.¹⁹² On this record, there is no legitimate

¹⁹¹ By its terms, Section 251(c) sets forth “Additional obligations of incumbent local exchange carriers.” The resale duty established in Section 251(c)(4) therefore applies only to ILECs.

¹⁹² See Ethernet LEADERBOARD.

basis for the Commission to conclude that any Ethernet provider has market power, and thus no basis for concluding that any provider can implement a successful price squeeze.

Nor is there any basis for the Commission to conclude that ILECs could implement a price squeeze for DS1 or DS3 services. As demonstrated above, the evidence shows that virtually every building where ILECs have demand for BDS, there is at least one other provider with nearby network facilities (or facilities at the same building). The only evidence of market power is the flawed regressions presented by Professor Rysman. But even if the Commission were to credit those regressions, they show that in non-competitive areas, ILEC prices are at most only about 3.2% above those in areas Professor Rysman deems to be “competitive.”¹⁹³

On this record, it is not at all surprising that the CLECs who seek these regulations have been unable to provide any actual evidence of the alleged price squeezes. Those seeking wholesale discounts have identified only isolated instances of alleged price squeezes, which AT&T has refuted. For example, AT&T has shown that Windstream’s allegations are highly

¹⁹³ In a competitive marketplace, providers cannot force wholesale customers to pay supra-competitive prices. As a result, the only way to implement a price squeeze would be to set retail prices *below* competitive levels. But that would be predatory pricing, and the Commission has repeatedly found that such vertical foreclosure predation claims are rarely credible in dynamic telecommunications markets. *See Applications for Consent to Transfer of Licenses*, 14 FCC Rcd. 3160, 3215, ¶ 118 n.327 (1999) (“We find that firms in dynamic industries such as telecommunications generally do not have the incentives to engage in predatory practices, because the success of such practices rests on a series of speculative assumptions.”); Report and Order and Order on Reconsideration, *Rules and Policies on Foreign Participation in the U.S. Telecomm. Market*, 12 FCC Rcd. 23891, 23979-80, ¶ 199, n.405 (1997); *see also Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588-91 (1986) (predatory conduct that requires profit sacrifice is “rarely tried, and even more rarely successful”). For example, the Commission has rejected claims that ILECs could use market power in local services to affect vertical price squeezes in downstream markets, where, as here, the presence of numerous established carriers with sunk investments in national networks rendered improbable any claim that an ILEC could recoup forgone profits. *See, e.g., SBC Application at 25737-8, ¶¶ 157-59; see also WorldCom*, 238 F.3d at 458-59. Similarly, in the antitrust context, the Supreme Court has rejected arguments that this type of “price squeeze” raises antitrust concerns. *Pac. Bell Tel. Co.*, 555 U.S. at 452 (rejected the plaintiffs’ “price squeeze” claim as “an amalgamation of a meritless claim at the retail level and a meritless claim at the wholesale level”).

misleading, given that Windstream’s comparisons are based on wholesale guidebook and tariffed rates, rather than the much lower wholesale prices that Windstream actually pays to AT&T under its commercial agreement with AT&T. Similarly, TDS has not provided any information to enable AT&T to verify its claims. Nonetheless, these allegations are refuted by the admission in May 2015 by the manager of commercial product management for TDS Telecom that, with respect to “AT&T’s Switched Ethernet,” TDS can “buy the service for a competitive price [and] make a few bucks on it.”¹⁹⁴

Even if true and verifiable, these isolated instances of alleged price squeezes do not establish the type of widespread conduct that could justify radical new regulations that would give wholesale customers their own lower rates. Rather, the CLECs have provided only localized instances of alleged price squeezes. To the extent that CLECs believe that wholesale prices for any specific location (or set of locations) are unreasonable, CLECs *already have a remedy*. BDS services are subject to the just and reasonable standard under Section 201(b) of the Act. Therefore, CLECs that believe that ILEC rates are unjust and unreasonable can already bring a Section 208 complaint with the Commission.

Finally, the Commission should reject proposals to separately regulate wholesale rates because such rules would impose enormous costs on the industry and retard continued investment and expansion of Ethernet facilities. Retail Ethernet services are typically sold as part of a larger bundle that includes multiple unregulated services. A requirement that the Ethernet transport component of these services be separately priced and tracked to facilitate the

¹⁹⁴ Sean Buckley, “TDS takes three-pronged approach to lighting business fiber,” FierceTelecom (May 12, 2015) (quoting Mark Lyons, TDS Telecom, manager of commercial product management), http://www.fiercetelecom.com/story/tds-takes-three-pronged-approach-lighting-business-fiber/2015-05-12?utm_campaign=AddThis&utm_medium=AddThis&utm_source=email#.VXBs6aqx2TM.email.

application of wholesale discounts would be costly. Nor is there any clear way to determine which purchasers are “wholesale” or “retail” for these purposes, and neither the carriers nor the Commission would have any administratively simple way to keep track of when a customer would be entitled to the discount and whether the customer is in fact using the service only for purposes approved for the “wholesale” discount.

Moreover, new regulations that would require BDS providers to offer their facilities to competitors at even lower rates would undermine facilities-based investment by both CLECs and ILECs, thus harming competition and consumers. Further reducing wholesale prices for BDS services could only further increase CLEC incentives to rely on ILEC-provided wholesale services rather than deploy their own facilities. At the same time, these regulations would create strong disincentives for ILECs to deploy Ethernet services to new locations, because the risk that they will have to sell those services at much lower wholesale prices will reduce the profitability of building out those facilities.¹⁹⁵ The result will be a slower transition to next generation services that have larger capacity and greater flexibility, which would only harm consumers and competition.

B. The Commission Should Not Issue Blanket Regulations Governing Terms And Conditions In Commercial Agreements And Tariffs.

The Commission should reject the proposals in the *Notice* to adopt *rules* that would prohibit certain terms and conditions for all commercial agreements, regardless of the circumstances or other provisions in those agreements. In promulgating a new rule, the Commission could prohibit only those provisions that are almost always and under almost all

¹⁹⁵ See, e.g., *United States Telecom Ass’n v. FCC*, 290 F.3d 415, 429 (D.C. Cir. 2002) (“As Justice Breyer’s separate opinion carefully explained, mandatory unbundling comes at a cost, including disincentives to research and development by both ILECs and CLECs and the tangled management inherent in shared use of a common resource. . . . [U]nbundling is not an unqualified good[.]”).

circumstances unlawful. Most of the issues raised in the *Notice* involve concerns expressed about particular terms or conditions contained in particular ILEC commercial contracts or tariffs, and that operate differently from ILEC-to-ILEC and from contract/tariff-to-contract/tariff. There is simply no basis in the record for the Commission to conclude that these provisions are generally unreasonable or anticompetitive. This point is starkly illustrated by the fact that some CLECs actually favor (or have in the past favored) some of the terms and conditions that other CLECs are asking the Commission to prohibit by rule. In all events, the terms and conditions raised in the *Notice* are clearly reasonable, and facilitate competition and the transition to IP-based services.

1. The Alleged Tying Provisions In Commercial Contracts.

The *Notice* asks whether the Commission should categorically declare unlawful and prohibit certain alleged “tying arrangements” contained in some commercial broadband service agreements.¹⁹⁶ The answer is no, for multiple reasons.

The Commission’s focus here is the claim of competitive LECs that “incumbent LECs use their market position in the TDM services [market] to leverage their sales of Ethernet services” through “different types of tying arrangements.”¹⁹⁷ Specifically, competitive LECs allege that incumbent LECs engage in tying through IP migration provisions, which “allow customers of [tariff pricing] plans to count their Ethernet purchases from the incumbent LEC toward fulfillment of their TDM pricing plan percentage commitments.”¹⁹⁸ Competitive LECs also allege that incumbent LECs engage in tying through volume-based commitments and accompanying penalty provisions. They claim that “incumbent LECs either waive or provide

¹⁹⁶ *Notice* ¶¶ 447-61.

¹⁹⁷ *Id.* ¶¶ 449, 451.

¹⁹⁸ *Id.* ¶ 451.

credit in a competitive LEC customer’s commercial agreement for Ethernet that offset that customer’s penalty liability under a tariff or non-tariff pricing plan as leverage to obtain the competitive LEC’s commitment to purchase the incumbent LEC’s Ethernet and other services.”¹⁹⁹ Finally, competitive LECs allege that incumbent LECs engage in “geographic tying,” *i.e.*, “tying the sale of business data services in markets where they have significant market share to the sale of business data services in markets where the Commission’s prior competitive triggers have been met.”²⁰⁰

The Commission’s suggestion that these arrangements “are harmful to competition in the business data services market” and will “inhibit the transition to IP technology”²⁰¹ gets it exactly wrong: these arrangements are not anticompetitive tying arrangements, and instead are pro-competitive and pro-IP transition. First, none of these arrangements is an actual “tying” arrangement under recognized legal and economic standards. A firm engages in tying when it has market power over one product and permits customers to purchase that product only if they also purchase a second product that could otherwise be purchased from competitors.²⁰² The concern with tying arrangements is that the firm with market power over the first product is leveraging that market power to gain market power over the second product, thus harming

¹⁹⁹ *Id.* ¶ 452.

²⁰⁰ *Id.* ¶ 457.

²⁰¹ *Id.* ¶ 447.

²⁰² See *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 461 (1992) (“A tying arrangement is ‘an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.’”) (quoting *N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 5-6 (1958)). Such an arrangement violates the antitrust laws “if the seller has ‘appreciable economic power’ in the tying product market and if the arrangement affects a substantial volume of commerce in the tied market.” *Eastman Kodak Co.*, 504 U.S. at 462 (quoting *Fortner Enters., Inc. v. United States Steel Corp.*, 394 U.S. 495, 503 (1969)).

competition and consumers in the marketplace for the second product.²⁰³ It follows that “where the buyer is free to take either product by itself there is no tying problem,”²⁰⁴ and that there is no tying problem “where the seller has no control or dominance over the tying product.”²⁰⁵

None of the challenged arrangements involves tying. IP migration provisions do not “condition” a customer’s purchase of TDM-based services on the customer’s agreement to purchase Ethernet services from AT&T (or to not purchase Ethernet services from other providers).²⁰⁶ Rather, these provisions merely permit customers who have long-term commitments to purchase TDM-based services from AT&T to instead *substitute* purchases of AT&T Ethernet services without incurring any penalties. Thus, AT&T’s TDM customers remain free to purchase no Ethernet services from AT&T, and also to purchase Ethernet services from other providers. Because customers are “free to take either [special access] product by itself” under the arrangement that AT&T offers, the products are not tied and “there is no tying problem.”²⁰⁷

Volume-based commitments also do not present any tying issues. These provisions are *optional* in the first place, and therefore cannot impose the “forced” consumer choices that are

²⁰³ See *N. Pac. Ry.*, 356 U.S. at 5 (“[Tying arrangements] deny competitors free access to the market for the tied product, not because the party imposing the tying requirements has a better product or a lower price but because of his power or leverage in another market. At the same time buyers are forced to forego their free choice between competing products.”); *Notice* ¶ 448.

²⁰⁴ *N. Pac. Ry.*, 356 U.S. at 6, n.4.

²⁰⁵ *Id.* at 6.

²⁰⁶ *Eastman Kodak*, 504 U.S. at 461; *cf. id.* at 463 (Kodak tied sales of service and parts because “[t]he record indicates that Kodak would sell parts to third parties *only if* they agreed not to buy service” from independent service organizations (emphasis added)); *Fortner Enters.*, 394 U.S. at 498 (holding that “a tying arrangement of the traditional kind” existed because defendant “sold its credit *only on the condition* that [plaintiff] purchase a certain number of prefabricated houses” from defendant (emphasis added)).

²⁰⁷ *N. Pac. Ry.*, 356 U.S. at 5 n.4.

the essence of tying arrangements.²⁰⁸ As with IP migration provisions, neither volume-commitments themselves nor the penalty provisions that accompany them “condition” a customer’s purchase of TDM-based services on the customer’s agreement to purchase Ethernet services from AT&T. The penalty provisions merely permit customers to offset penalty liability that they would otherwise incur under TDM-based volume commitments if they choose to purchase AT&T’s Ethernet services. There is no requirement, however, that customers purchase AT&T’s Ethernet services at all and they remain free to purchase Ethernet services from AT&T’s competitors.

Even if the challenged arrangements attempt to “tie” purchases of AT&T’s TDM-based products to its Ethernet products – and they do not – the market conditions that are a prerequisite to successful tying arrangements are absent here. As noted, market power in the “tying product” market is a “necessary feature” of an illegal tying arrangement.²⁰⁹ Without such market power, the seller’s attempt to force its customers to buy the tied product along with the tying product will inevitably fail, because customers will simply buy the tying product from available competitors who offer it by itself.²¹⁰ As shown above, the record overwhelmingly demonstrates the absence of market power for BDS. Accordingly, the *Notice*’s suggestion that the challenged arrangements are anticompetitive is incorrect.

The record also refutes the competitive LECs’ assertion that incumbent LECs engage in “geographic tying” by tying the sale of TDM-based services in non-competitive markets (mainly rural areas) to the sale of such services in competitive markets. AT&T demonstrated in its Direct

²⁰⁸ *Id.* at 6; *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 12 (1984).

²⁰⁹ *Eastman Kodak*, 504 U.S. at 464.

²¹⁰ *N. Pac. Ry.*, 356 U.S. at 7 (“[I]f one of a dozen food stores in a community were to refuse to sell flour unless the buyer also took sugar it would hardly tend to restrain competition in sugar if its competitors were ready and able to sell flour by itself.”).

Case submission in the *Tariff Investigation* that in order to leverage sales in non-competitive areas to exercise market power in competitive areas, it would have to have very substantial sales in the non-competitive areas, which is not plausible because most special access demand is concentrated in the densely-populated areas that are the most competitive.²¹¹

Finally, the Commission undercuts its own analysis on this issue by acknowledging that “linking DSn purchases and Ethernet purchases involves material short term benefits for purchasers as they attempt to manage the effects of the decline in TDM services and the transition to IP services.”²¹² The Commission is correct that the challenged provisions are pro-competitive and serve to facilitate the transition to IP. The IP migration provisions permit customers who have long-term commitments to purchase TDM-based services from AT&T to instead substitute purchases of AT&T Ethernet services without incurring any penalties. Absent these provisions, customers would have to either continue using TDM services or incur the agreed-upon early termination charges. The volume commitments and accompanying penalty provisions similarly provide customers with *additional* flexibility to manage their transition to IP services.

The pro-competitive benefits of these arrangements are confirmed by the fact that CLECs are divided on them, with “[s]ome competitive LECs advocat[ing] in favor of such

²¹¹ See Brief of AT&T in Support of its Direct Case, *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans*, WC Docket No. 15-247, at 36-37 (filed Jan. 8, 2016) (“AT&T Direct Case”) (“There is no plausible basis to conclude that a firm can leverage market power in areas that account for a very small fraction of demand into the areas where the great majority of the demand is.”).

²¹² *Notice* ¶ 459; see also *id.* (“Considering the benefits of these arrangements may be particularly relevant given the current decline in TDM sales and the consequent penalty liabilities that decline involves.”).

arrangements.”²¹³ The fact that some CLECs are asking the FCC to *require* such provisions, while others are asking the FCC to declare them unlawful, shows that at least some CLECs view them as a welcome option as they navigate the technology transition. The Commission therefore would disserve its own objective of facilitating that transition if it prohibited the challenged provisions. A prohibition would foreclose CLECs from reaping the benefits of these provisions, without preventing any competitive harms (since there are none). Such a regulatory action therefore would be unwise as well as unwarranted.

2. The Commission Should Not Regulate Percentage Commitments, Term Commitments, Upper Percentage Thresholds, Or Overage Charges.

The Commission should also reject the proposals in the *Notice* to adopt *rules* that would prohibit or otherwise restrict the use of percentage commitments, term commitments, upper percentage thresholds, or overage penalties in all BDS agreements, regardless of the level of competition in the market, the individual circumstances and needs of the parties, or the other provisions in the agreement.²¹⁴

As an initial matter, there is clearly no need for the Commission to regulate these provisions in markets it finds are competitive.²¹⁵ In competitive markets, consumers are, by definition, already protected by the presence of competition, and so it would be unnecessary, if not harmful, for the Commission to substitute its judgment regarding the appropriateness of these terms for the judgment of the actual participants in the market. As the *Notice* itself acknowledges, “[w]here competition exists, there is little for government to do except to

²¹³ *Id.*; see also *id.* at ¶ 455 (“Competitive LECs take two positions in connection with [IP migration] provisions.”).

²¹⁴ See *id.* ¶¶ 321-43.

²¹⁵ See *id.* ¶ 322 (requesting comment on whether the Commission should regulate the terms and conditions of BDS agreements “solely [in] noncompetitive markets or [in] all markets”).

maintain the traditional oversight of telecommunications services, because competition is the single best way of ensuring that customers benefit.”²¹⁶ The participants in the BDS market are sophisticated buyers and sellers of communications services, and to the extent that they determine, after exploring competitive alternatives, that these provisions meet their needs, there is no rational basis for the Commission to interfere with that decision. Complaint proceedings would continue to be available as needed, which further diminishes the need for rules regulating these terms in competitive markets.

Moreover, even in markets the Competitive Market Test deems “non-competitive,” it would be inappropriate, on this record, for the Commission to adopt *rules* restricting the usage of these types of contract provisions. In order to promulgate universally-applicable rules regulating the use of these types of provisions, the Commission would need to show that they are almost always, and under almost all circumstances, unlawful. The Commission’s finding in the *Tariff Investigation Order* was merely that certain uses of these terms were unlawful and anticompetitive *as they were used in the specific tariffed portability plans that were at issue in that investigation*. But there is no basis in the current record for the Commission to conclude that this is *universally* so in all BDS agreements.

Indeed, there are many scenarios in which sophisticated BDS purchasers and sellers might legitimately determine that the provisions that the Commission found unlawful in the context of *Tariff Investigation Order* are pro-competitive. These types of scenarios are not difficult to imagine. For example, assume that an Ethernet provider is willing to offer lower rates to a purchaser that agrees to certain percentage commitments, shortfall charges, and early termination fees above expectation damages because this will result in more predictable network

²¹⁶ *Id.* ¶ 5.

usage, recovery of capital expenditures for any necessary network build, and stable revenue over the course of the agreement. And assume also that the customer reasonably anticipates that its need for Ethernet services will gradually increase over the next five years, and so it is willing to agree to these provisions in exchange for a reduction in rates or other concessions from the seller (e.g., facilities build, enhanced SLAs). Under these circumstances, the parties could reasonably determine that it is not unreasonable to incorporate shortfall or early termination clauses similar to those that the Commission found to be unlawful under the unique circumstances that were at issue in the *Tariff Investigation Order*.

To be sure, the record in the *Tariff Investigation Order* showed that these provisions do not harm consumers or otherwise impede the IP transition. For example, in its comments on the *Tariff Investigation Order*, AT&T showed that most of the CLECs that subscribed to the AT&T portability plans at issue enjoyed substantial “headroom” under their agreements and could immediately move a substantial volume of circuits away from AT&T and to a competitor without incurring any shortfall charges or early termination liability.²¹⁷ Because these customers had such substantial headroom, they could have immediately canceled a significant number of channel terminations early without incurring any early termination fees. Thus, at least with respect to these customers, shortfall charges and early termination liabilities were not preventing them from moving their services to competitors or impeding their transition to IP services.

Simply put, there are any number of market scenarios in which these types of clauses can be included in BDS agreements without causing competitive harm or slowing the IP transition. Thus, even assuming that there might be some specific circumstances in which the use of these provisions might be harmful, the Commission cannot say, based on the current record, that this

²¹⁷ AT&T Direct Case at 21-22.

will be so in almost all (or even most) circumstances. Thus, to the extent that parties choose to incorporate these provisions into their agreements, the Commission has not shown why they should be barred from doing so by a one-size-fits-all prohibition. Moreover, the complaint process will remain available to address individual instances where these provisions might be unjust or unreasonable, which further mitigates against the need for the Commission’s proposed one-size-fits-all proscription on these provisions.

C. The Commission’s Proposal to “Detariff” TDM Services In Name Only Would be Unlawful.

The Commission proposes to retain price cap regulation in the areas the Competitive Market Test deems to be “non-competitive.”²¹⁸ But the Commission also proposes to “deregulate” the pricing process, by effectively extending Phase I relief (*i.e.*, greater flexibility in negotiating contracts) to all “non-competitive” areas and detariffing all legacy TDM services “while maintaining price cap regulation on a detariffed basis.”²¹⁹ Although most of these proposed measures to deregulate TDM services are sound, the method in which the Commission is proposing to forbear from tariff requirements for TDM services in non-competitive areas would paradoxically (and unlawfully) increase the Commission’s authority beyond what the statute currently permits.

The Commission is actually proposing a kind of “faux” detariffing in which price cap LECs like AT&T would be subject to all of the obligations but none of the carrier protections of the tariffing regime. Although the Commission indicates that it will issue a forbearance ruling detariffing all TDM BDS services, the *Notice* proposes to readopt most of the ILECs’ obligations under the tariffing system in slightly different form. Price cap LECs will still be subject to the

²¹⁸ *Notice* ¶ 351.

²¹⁹ *Id.* ¶ 497.

full price cap regime of *ex ante* rate regulation; they would have to publish their rates and terms essentially as before, albeit on the Internet; and they would have to file the same types of support for its rates, to permit the Commission to assess compliance with the price cap rules. But because the Commission proposes to remove the requirement of a formal tariff, the Commission would in effect be forbearing from the limitations on its own power to review ILEC rates, embodied in such provisions as the “deemed lawful” provisions of Section 204 and the prescription provisions of Section 205. Such an approach would be unlawful; the Commission cannot, in effect, lawfully “forbear” only from the limitations on its own power, while retaining essentially all of the carrier burdens of a tariffing regime.

VI. THE COMMISSION’S PROPOSALS FOR REGULATION IN “COMPETITIVE” AREAS WOULD BE UNLAWFUL AND UNSUPPORTED.

The *Notice* seeks comment on whether the Commission should impose intrusive regulations governing terms and conditions in commercial agreements and tariffs governing the sale of BDS in *competitive* areas. The answer is clearly no. By definition, competition will ensure that the terms and conditions governing the sale of BDS are just and reasonable. Prohibitions on the use of particular terms and conditions could only reduce the tools available to buyers and sellers of BDS in competitive markets that could be used to develop innovative and mutually beneficial arrangements for BDS, and thus by definition could only undermine the implementation of the most customer-friendly arrangements.

A. Non-Disclosure Arrangements.

The *Notice* proposes to prohibit Non-Disclosure Agreements (“NDAs”) that restrict BDS purchasers and providers from sharing information with the Commission or other government agencies, including even NDAs that expressly allow information to be shared when required by

law, legal process, or regulatory authority.²²⁰ The proposed rules would, in effect, allow parties to “voluntar[ily]” disclose protected information to the Commission and other agencies, notwithstanding the existence of an NDA.²²¹

These proposed restrictions on the enforceability of NDAs are unnecessary and undermine the legitimate confidentiality needs of participants in the BDS market. As the Commission itself acknowledges in the *Notice*, NDAs play an “important role . . . in ensuring the protection of confidential information in commercial agreements,” and “[p]arties to a commercial agreement have the right to seek protection of their confidential information and would be unlikely to enter into such commercial agreements without reasonable assurance that their sensitive business information would not be compromised.”²²² It should go without saying that the terms and conditions that AT&T – or, for that matter, any other BDS purchaser or provider – includes in its commercial proposals and agreements are highly confidential, and the public release of this information would result in significant competitive harm, especially during contract negotiations with other parties.

The Commission has not shown that there is a need for the rules it has proposed. In AT&T’s experience, the overwhelming majority of the NDAs in BDS agreements already allow the disclosure of confidential information *when required by law, government authority, or legal process*. Thus, the Commission can, when needed, issue an express direction to the parties to provide whatever information the Commission needs regarding their agreements, including copies of the underlying agreements themselves and any related information, precisely as it did

²²⁰ *Id.* ¶¶ 316-17.

²²¹ *Id.* ¶ 318.

²²² *Id.* ¶ 319.

in the *Tariff Investigation Designation Order*.²²³ AT&T believes that this remedy, which is already being implemented in the marketplace, strikes the proper balance. It gives the Commission the opportunity to obtain the information that it reasonably needs to perform its statutory duties, while also ensuring that information which is legitimately protected by an NDA will be provided to the Commission only when *the Commission* considers it to be appropriate, and in an orderly manner (*e.g.*, after a protective order has been issued), rather than simply at the whim of any one market participant and without notice to or knowledge of the other participant whose confidential information is actually being shared.²²⁴

In the *Notice*, the Commission suggests that this approach “unduly restricts” its access to information because the Commission “can only access information it specifically seeks, the existence and substance of which the parties are bound not to disclose[.]”²²⁵ This concern is overstated, and the *Notice* fails to identify a single instance where it has actually requested a contract pertaining to BDS and the parties refused to provide it.

B. The Commission Should Not Extend The Prohibitions Adopted In The Tariff Investigation Proceedings To Other Agreements And Tariffs.

The *Notice* seeks comment on whether to extend to all agreements for BDS in all areas the prohibitions adopted for the tariffs subject to the *Tariff Investigation Order*. The answer is clearly no. As noted, absent a finding that such provisions are generally unreasonable in most circumstances, such a prohibition would cause competitive harm by reducing industry flexibility

²²³ Order Initiating Investigation and Designating Issues for Investigation, *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans*, WC Docket No. 15-247, ¶ 105 (rel. Oct. 16, 2015).

²²⁴ Naturally, the Commission could reiterate that contracts between private parties would not defeat the Commission’s (or any other government agency’s) authority to compel production of such agreements under authority of law.

²²⁵ *Notice* ¶ 317.

to implement pro-competitive arrangements. There is no evidence in the record that “all or nothing” arrangements, or termination liability that exceeds the cost of simply completing the plan are unlawful in all contexts. Indeed, even under the tariffs subject to the investigation, there were no serious claims that such provisions were unlawful when customers were experiencing substantial growth in TDM-based services and thus realized only the benefits of those agreements (lower prices and greater flexibility) without any of the downsides that occurred as demand for TDM-based services began to dry up. Accordingly, the Commission should do as it has done in the past: regulate terms and conditions with a light touch, and address issues only as they arise in tariff investigation and complaint proceedings.

CONCLUSION

For the foregoing reasons, the Commission should resolve this proceeding in the manner described above.

Respectfully submitted,

James P. Young
Christopher T. Shenk
Jacqueline G. Cooper
Kyle J. Fiet
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000

/s/ Keith Krom
Keith Krom
Gary L. Phillips
David L. Lawson
AT&T Inc.
1120 20th Street, N.W.
Washington, D.C. 20036
(202) 457-3058

Attorneys for AT&T Inc.

June 28, 2016