



October 7, 2016

Ex Parte

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: *Business Data Services in an Internet Protocol Environment (WC Docket No. 16-143); Special Access 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 Service (RM-10593)*

Dear Ms. Dortch:

For nearly a decade, certain parties advocating for expanded regulation of Business Data Services (BDS) have repeated a statistic stating that BDS-provided backhaul used in Sprint's wireless network accounts for approximately one-third of the "cost of operating of a cell site."¹ The Commission itself has cited this figure.² The statistic, however, is misleading; the source data are a decade old and the figure dramatically overstates the impact of BDS on overall wireless costs. More important, the portion of wireless costs attributable to backhaul is irrelevant to questions of economic efficiency or market power because it says nothing about the competitiveness of the marketplace. Therefore, it fails to offer a basis for any new BDS regulation, and in any event the Commission cannot justify new BDS regulation based on claims that backhaul represents some portion of one company's 2006 cell site operating costs.

¹ See, e.g., *Comments of Competitive Carriers Association*, WC Docket Nos. 16-153, 15-247, 05-25, and RM-10593 (Jun. 29, 2016) at 16 available at <https://ecfsapi.fcc.gov/file/10628249519542/CCA%20BDS%20Comments%20vFINAL.pdf>.

² Federal Communications Commission ("FCC"), *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993 – Annual Report and Analysis of Competitive Market Conditions With Respect to Mobile Wireless, Including Commercial Mobile Services, Eighteenth Report* at ¶169 (Dec. 23, 2015) available at https://apps.fcc.gov/edocs_public/attachmatch/DA-15-1487A1.pdf and Tom Wheeler, Chairman, FCC, *Prepared Remarks on "The Future of Wireless: A Vision for U.S. Leadership in a 5G World" at the National Press Club* at 6 (Jun. 20, 2016), available at https://apps.fcc.gov/edocs_public/attachmatch/DOC-339920A1.pdf.

First, as noted above, the source data for the backhaul costs cited are from 2006.³ During the decade that has passed, wireless carriers across the industry, including Sprint, have upgraded their networks with higher-capacity, more efficient backhaul to support fourth generation wireless data services. Thus, even if the statistic was an accurate reflection of network operating costs at that time, there is no evidence that today's network operating costs are the same. The Commission cannot rely on such clearly outdated data.

Second, even if the portion of cell site operating costs attributable to backhaul for Sprint were one-third today, reliance on that figure to justify lowering BDS prices vastly overstates the impact of backhaul costs on overall wireless costs. Backhaul represents a much lower percentage share of total wireless operating costs because cell site operating costs comprise only a portion of service costs, which are in turn only a portion of total operating costs.

To illustrate, a review of Sprint's most recent annual financial statements indicate that total wireless segment operating costs of \$29.9 Billion for the Fiscal Year Ended March 31, 2016 included the following categories:⁴

- Cost of services: \$8.1 Billion (27 percent)
- Cost of products: \$5.8 Billion (19 percent)
- Selling, general, and administrative: \$8.1 Billion (27 percent)
- Depreciation: \$5.6 Billion (19 percent)
- Amortization: \$1.3 Billion (4 percent)
- Other: \$1.0 Billion (3 percent)

Backhaul costs represent some portion of the 27 percent of costs that are "costs of services." Costs of service include the following items according to the Sprint Fiscal 2015 10K:⁵

- Fixed and variable interconnection costs, the fixed component of which consists of monthly flat-rate fees for facilities leased from local exchange

³ See *Comments of Sprint Nextel Corporation*, WC Docket No. 05-25 and RM 10593 (Aug. 8, 2007) at 33, available at <https://ecfsapi.fcc.gov/file/6519610326.pdf>, and Attachment I at 3, available at <https://ecfsapi.fcc.gov/file/6519610327.pdf>.

⁴ Sprint Investor Relations, *Financial, Financial and Operating Information – Excel for the Quarter Ended FY2015 3/13/16* (May 2016) at Wireless SoP tab, available at <http://investors.sprint.com/financials/default.aspx>. Fiscal year totals are the sum of the corresponding figures for the four quarters ending March 31, 2016.

⁵ Sprint Corporation, *Form 10K: Annual Report Pursuant To Section 13 or 15(D) of the Securities Exchange Act of 1934 for Fiscal Year Ended March 31, 2016* (May 17, 2016) ("Sprint Fiscal 2015 Form 10K") at 42, available at <http://d1lge852tjjqow.cloudfront.net/CIK-0000101830/fb6f230b-631d-4f15-bb0a-110f281b3fde.pdf>.

carriers and other providers based on the number of cell sites and switches in service in a particular period and the related equipment installed at each site, and the variable component of which generally consists of per-minute use fees charged by wireline providers for calls terminating on their networks, which fluctuate in relation to the level and duration of those terminating calls.

- Costs to operate and maintain our networks, including direct switch and cell site costs, such as rent, utilities, maintenance, labor costs associated with network employees, and spectrum frequency leasing costs.
- Long distance costs paid to [Sprint's] Wireline segment; roaming fees paid to other carriers; regulatory fees; costs to service and repair devices; and fixed and variable costs relating to payments to third parties for the subscriber use of their proprietary data applications, such as messaging, music and cloud services and connected vehicle fees.

Backhaul likely falls in the category listed as “monthly flat-rate fees for facilities leased from local exchange carriers and other providers based on the number of cell sites and switches in service in a particular period and the related equipment installed at each site.” The company does not break out the amounts for each subcategory of cost of services, which are too small individually to warrant reporting. But since the cost of operating cell sites is a subset of the cost of services, we can get an upper bound by taking one-third of the cost of services. This would imply a backhaul share of no more than 9 percent (27 percent * 33 percent), but likely much lower since, as shown above, there are services costs in addition to those for operating cell sites, e.g., device service and repair; long distance, roaming, and traffic termination charges; regulatory fees; and content costs. A paper recently submitted in the BDS docket on behalf of the Competitive Carriers Association (CCA) provides confirmation: it estimates that the portion of *total* operating expenses attributable to backhaul for Sprint, T-Mobile, US Cellular, and nTelos is between 2 percent to 6 percent, with an average of about 4 percent.⁶ Of course, the share provided by incumbent local exchange carriers will be lower still, as Sprint purchases from “local exchange carriers,” which presumably include both incumbent and competitive local exchange carriers, and “other providers,” presumably cable operators and fiber providers such as Zayo and FiberTower.

⁶ Raul Katz, Telecom Advisory Services, LLC, *Assessment of the Impact of the Business Data Services Market Dynamics on Innovation and Competition in the US Wireless Market* (July 2016) (“CCA Paper”) at 20-22 available at <http://cca-convention.org/wp-content/uploads/2016/08/Katz-Study-vFinal.pdf>. The paper also estimates backhaul costs for Cincinnati Bell Wireless, which is no longer operating, and Cricket, which was acquired by AT&T. To be clear, USTelecom disagrees with much of the analysis and the conclusions of the CCA Paper, despite its more realistic treatment of backhaul costs.

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While it is easy to get caught up in the details of the backhaul cost calculation, it is perhaps more important to step back and assess the usefulness of the exercise. One quickly realizes that the share of costs attributable to backhaul is utterly irrelevant to the fundamental questions of economic efficiency and market power. The relevant question is whether the service is supplied competitively. The Commission cannot take regulatory action based on a premise that the share of costs attributable to a particular input – especially one particular company's costs – justifies BDS price reductions across the board.

Sincerely,

A handwritten signature in cursive script that reads "Jonathan Banks". The signature is written in black ink on a white background.

Jonathan Banks
Patrick S. Brogan