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August 9, 2016

REDACTED – FOR PUBLIC INSPECTION

By ECFS

Marlene H. Dortch
Office of the Secretary
Federal Communications Commission
455 12th Street, S.W.
Washington, DC 20054

Re: WC Docket Nos. 16-143, 15-247, 05-25, RM-10593; **Public** Version of the Reply
Comments of AT&T Inc.

Dear Ms. Dortch:

Pursuant to the *Protective Orders* adopted by the Commission in WC Docket Nos. 16-143, 15-247, 05-25, and RM-10593,¹ AT&T Inc. respectfully submits the enclosed **Public** version of its Reply Comments in these proceedings. We are concurrently filing a Highly Confidential version of these Reply Comments via hand delivery.

Individuals who are admitted to the *Protective Orders* in these proceedings can request an unredacted copy of this document by contacting Kyle Fiet of Sidley Austin LLP (kfiet@sidley.com).

Respectfully submitted,

/s/ Kyle J. Fiet

Kyle J. Fiet

Enclosure

¹ See Order, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593 (rel. Jun. 24, 2016) (collecting citations for the protective orders previously issued in these proceedings).

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of)	
)	
Business Data Services in an Internet)	WC Docket No. 16-143
Protocol Environment)	
)	
Investigation of Certain Price Cap Local)	WC Docket No. 15-247
Exchange Carrier Business Data Services)	
Tariff Pricing Plans)	
)	
Special Access Rates for Price Cap Local)	WC Docket No. 05-25
Exchange Carriers)	
)	
AT&T Corp. Petition for Rulemaking to)	RM-10593
Reform Regulation of Incumbent Local)	
Exchange Carrier Rates for Interstate)	
Special Access Services)	

REPLY COMMENTS OF AT&T INC.

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August 9, 2016

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Before the
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In the Matter of)	
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)	
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
)	

REPLY COMMENTS OF AT&T INC.

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

INTRODUCTION AND SUMMARY

The Commission promised that this rulemaking would be a data-driven inquiry, based on what is likely the largest data collection in the agency’s history. This data collection provides incontrovertible evidence that competition for Business Data Services (“BDS”) is robust and

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 Service*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (rel. May 2, 2016) (“Notice”).

nearly ubiquitous. Yet, instead of following this evidence, CLECs pretend it does not exist and urge the Commission to continue down the same road to intrusive, investment-killing reregulation on which it embarked before the data were in and properly analyzed. To that end, they submit proposals cynically described as “compromise” proposals that reflect nothing more than minor horse trading among those whose interests are aligned.

It is time to reset the conversation and get back to data-driven decision making. The Commission may have initiated this proceeding believing in good faith that competition for BDS outside of major metropolitan areas is lacking, but the data show otherwise. In fact, the data show that, as of 2013, competitors had deployed competing facilities in more than 95 percent of census blocks with BDS demand in MSAs, and that those census blocks cover 97 percent of the BDS connections and 99 percent of business establishments in MSAs.² To put this in perspective, the median size of a census block in an MSA is less than 0.02 square miles (less

² Mark Israel, Daniel Rubinfeld & Glenn Woroch, Competitive Analysis of the FCC’s Special Access Data Collection: White Paper, *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 Service*, WC Docket No. 05-26, RM-10593, at 16-17 (Jan. 28, 2016) (“IRW First White Paper”); Mark Israel, Daniel Rubinfeld & Glenn Woroch, Analysis of the Regressions and Other Data Relied Upon in the Business Data Services FNPRM And a Proposed Competitive Market Test: Second White Paper, *Business Data Services in an Internet Protocol Environment; 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 Service*, WC Docket Nos. 16-143, 05-25, RM-10593, at 1 (June 28, 2016) (“IRW Second White Paper”); Mark Israel, Daniel Rubinfeld & Glenn Woroch, Analysis of the Regressions and Other Data Relied Upon in the Business Data Services FNPRM And a Proposed Competitive Market Test: Third White Paper, *Business Data Services in an Internet Protocol Environment; 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 Service*, WC Docket Nos. 16-143, 05-25, RM-10593, at 3 (Aug. 9, 2016) (“IRW Third White Paper”); *see also* Notice ¶ 171. The results are very similar even when cable HFC-based offerings (including both “best efforts” and Ethernet over HFC) are omitted. IRW First White Paper at 15, tbl. F-REG (showing that competitive facilities have been deployed in 93.1 percent of census blocks in Phase II MSAs, 92.4% of census blocks in Phase I MSAs, and 84.5% of census blocks in Price Cap MSAs).

than 1,000 feet across), and the *Notice* recognizes that “fiber-based competitive supply within at least half a mile generally has a material effect on prices of BDS,”³ and almost all BDS demand is well within a half mile of competitive facilities: in the case of AT&T, 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.⁴ Indeed, on average, buildings with BDS demand are either connected to or within about *364 feet* of competitive fiber; three quarters of them are within 456 feet of competitive fiber; and about *half* of these buildings are within only *88 feet* of competitive fiber facilities.⁵

The same is true when the universe is limited to sub-50 Mbps connections: ninety percent of AT&T’s sub-50 Mbps bandwidth is within a half mile of competitive fiber.⁶ And CLECs not only have the facilities to compete for all BDS demand, but have been quite successful in winning business. According to the *Notice*, even as of 2013, competitors accounted for a majority of BDS revenue – without even taking cable into account.⁷ Competitors’ market share is undoubtedly higher today.

³ *Notice* ¶ 161.

⁴ IRW Second White Paper at 5.

⁵ See Second Supplemental Declaration of Mark Israel, Daniel Rubinfeld & Glenn Woroch, ¶ 5 (Apr. 20, 2016) (“IRW Second Supp. Decl.”), attached to Letter from Christopher T. Shenk (AT&T) to Marlene H. Dortch (FCC), *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 (Apr. 20, 2016); see also *id.* ¶ 6 (“virtually all of these buildings are within 0.5 miles of competitive fiber”).

⁶ IRW Second White Paper at 5.

⁷ *Notice* ¶ 217, fig. 9.

These data should be dispositive. The economic testimony⁸ and both the Commission and the D.C. Circuit⁹ have recognized that once competitors have deployed their own sunk facilities, incumbent LECs cannot engage in anticompetitive pricing.

Yet despite this evidence of near-ubiquitous CLEC facilities and marketplace success, the Commission purports to find evidence of significant ILEC market power in regression analyses conducted by Professor Rysman and then revised by Commission Staff in response to criticisms of Professor Rysman’s analyses in peer reviews. There is no such evidence.

First, even taking the results of these analyses at face value and ignoring their serious methodological flaws, discussed below, they do not demonstrate any cognizable level of market power. In fact, the regressions specifically tested for and found *no* evidence of market power in any service – Ethernet or TDM – above 50 Mbps.¹⁰ And although neither Professor Rysman nor Commission Staff report regression results for Ethernet services below 50 Mbps, Drs. Israel,

⁸ See, e.g., IRW First White Paper at 6-8; IRW Second White Paper at 39-40; IRW Third White Paper at 2.

⁹ See, e.g., *WorldCom, Inc. v. FCC*, 238 F.3d 449, 458-59 (D.C. Cir. 2001) (“[T]he presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed”); Fifth Report & Order & Further Notice of Proposed Rulemaking, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, 14 FCC Rcd. 14221, ¶ 80 (1999) (“*Pricing Flexibility Order*”) (same); Order on Remand, *Unbundled Access to Network Elements, Unbundled Access*, 20 FCC Rcd. 2533, ¶ 63 (2004) (“*Unbundled Access Order*”) (recognizing that “facilities-based competition” is the “most effective discipline to anticompetitive price squeezes”).

¹⁰ Dr. Marc Rysman, *Empirics of Business Data Services: White Paper*, at 3, 23-24 (Apr. 2016) (revised June 2016) (“Rysman White Paper”) (“I do not detect an effect of competition for high bandwidth lines . . .”), available at https://apps.fcc.gov/edocs_public/attachmatch/DOC-340040A6.pdf; Notice ¶ 244; Peer Review of *Empirics of Business Data Services* White Paper by Dr. Marc Rysman (April 2016), *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, Attachments 1-3 (June 28, 2016) (“Commission Staff Response”), available at http://transition.fcc.gov/Daily_Releases/Daily_Business/2016/db0708/DOC-340040A8.pdf.

Rubinfeld, and Woroch took Professor Rysman’s regression models and ran them for those services, and the results were the same – no evidence of market power.¹¹ Thus, these regressions produce *zero* evidence of any market power in services above 50 Mbps and in any Ethernet service, regardless of bandwidth.

With respect to DS1 and DS3 services, the results are not as stark but they clearly belie the claims of broad-based market power underpinning proposals for radical reregulation. While Professor Rysman’s initial regressions contain some mixed results that could be taken to suggest that ILECs might have (very limited) market power in some circumstances for legacy DS1 and DS3 services, when the Commission Staff re-ran them to meet the peer reviewers’ criticisms, many of those results became statistically insignificant, particularly for DS3 services.¹² And when Drs. Israel, Rubinfeld, and Woroch re-ran them again to correct the method used to compute clustered standard errors, consistent with the peer reviews, they became even more so; in fact nearly *all* of the DS3 results became statistically insignificant.¹³ Moreover, even to the limited extent the results could be read to suggest the presence of some market power for DS1 services in some areas, the observed pricing effects are barely cognizable – typically only about three percent.¹⁴

Given these results, the so-called “compromises” that are being presented to the Commission – which would, among other things, regulate Ethernet and significantly reduce prices for DS1 and DS3 services – should be dead on arrival. Nothing in these results supports the sweeping conclusion that that ILECs possess market power for *all* BDS below 50 Mbps;

¹¹ IRW Second White Paper at 25-26.

¹² *See, e.g.*, Commission Staff Response, Attachments 1-3.

¹³ *See* IRW Third White Paper at 14-15, 22-25.

¹⁴ *Id.* at 26; *see also* IRW Second White Paper at 20-21.

nothing supports the “built for failure” tests of market power for services above 50 Mbps; and certainly nothing remotely supports the dramatic one-time price reductions and X-factor revisions set forth in these self-serving proposals.

That the regressions showed so little evidence of market power is all the more noteworthy because the methodology and data used for those analyses were biased to *overstate* the presence of market power. One reason, as AT&T and others, including the peer reviewers, showed earlier, is that they erroneously equate correlation with causation. As a result of this fundamental “endogeneity” problem, the regressions cannot tell us whether the observed pricing effects are due to the existence of market power or to other unrelated factors, including the quite obvious reality that competitors are naturally drawn to the areas where demand is greatest and deployment costs (and hence prices) are lowest. Professor Rysman conceded this problem with his initial regressions, and, as the peer reviewers note, neither his nor Staff’s attempts to adjust for it cured the problem because the Commission lacks the information needed to do so.¹⁵

But this is not the only serious bias in the results. For example, many of the prices in the data set were established in long-term agreements negotiated prior to 2013 and thus could not logically have been “caused” or influenced by competitive conditions in 2013. Professor Mayo has presented regression results showing that, when matching 2013 competitive conditions with

¹⁵ See, e.g., IRW Second White Paper at 9-17; IRW Third White Paper at 15-19; Andrew Sweeting, Review of Dr. Rysman’s “Empirics of Business Data Services” White Paper, ¶¶ 19-20 (Apr. 26, 2016) (“Sweeting First Review”), available at https://apps.fcc.gov/edocs_public/attachmatch/DOC-340040A4.pdf; Letter from Tommaso Valletti (Imperial College London) to Matthew DelNero (FCC) at 6 (Apr. 28, 2016) (“Valletti First Review”), available at https://apps.fcc.gov/edocs_public/attachmatch/DOC-340040A5.pdf.

prices in 2013 contracts, the regressions no longer indicate market power, even for DS1 and DS3 services.¹⁶

Likewise, many of the prices used in the regressions are obviously incorrect, including, for example, data points with DS1 circuit prices exceeding \$100,000, even though DS1 prices in the real world are in the \$200-\$400 range.¹⁷ The regressions also incorrectly rely on pricing data only for circuits with the same bandwidth for all components of the circuit (*e.g.*, channel termination and transport), thus systematically excluding lower priced circuits that rely on multiplexing (*e.g.*, DS3 transport facilities multiplexed to DS1 channel terminations).¹⁸ Further, the data used in the regressions exclude about 42 percent of the buildings in a non-random fashion, due to limitations in the underlying dataset.¹⁹ And, of course, the regressions do not account for enormous expansion of competitors' facilities-based BDS networks since 2013.

Given these serious flaws, and that even ignoring these flaws, the data do not support the kinds of proposals advanced in the *Notice*, it is time for a reset. Rather than plow ahead with an outcome that is unsupported by the facts, the Commission must recognize that the current record compels the following fundamental conclusions. Any other outcome would be patently arbitrary and capricious.

¹⁶ See Declaration of John W. Mayo, ¶ 71 (June 28, 2016) (“Mayo Decl.”), attached as Exhibit B to the Comments of Comcast Corp., *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593 (June 28, 2016) (“Comcast 6/28 Comments”).

¹⁷ See IRW Second White Paper at 17-19.

¹⁸ *Id.*

¹⁹ *Id.*

First, there is no basis for new ex ante rate regulation of Ethernet services. The Commission determined many years ago that the marketplace for Ethernet services is highly competitive and that there is thus no legitimate basis for *ex ante* regulation of Ethernet services. To reverse course now, the Commission must surmount a high bar and provide an especially “detailed justification” showing that regulatory intervention is affirmatively necessary in light of changed circumstances, *i.e.*, that the Ethernet marketplace is no longer as competitive as it was in 2007.²⁰ The record cannot support such a showing. As noted, neither Professor Rysman nor the Commission Staff found any evidence in the regressions to indicate market power for any Ethernet services. This should come as no surprise because the structure of the Ethernet marketplace ensures competition. There are literally dozens of non-ILEC providers of Ethernet services, and no provider has a port share that exceeds one-fifth of the market. Nine providers have port shares of four percent or more, including three CLECs, and three of the nation’s largest cable companies. Moreover, the marketplace exhibits all of the core hallmarks of a competitive market: skyrocketing demand, output, and investment, coupled with plummeting prices. On this record there is no non-arbitrary basis for the Commission to conclude that the market is less competitive today than in 2007, and there is thus no justification for reregulating these services at all.

Second, there is no evidentiary basis for proposals to reregulate DS1 and DS3 Services in all areas of the country. While there is no basis in the record for reregulation of any Ethernet service or any service above 50 Mbps, Staff’s regressions purport to find limited evidence of market power for DS1 services and mixed results for DS3 services. Although even this limited evidence largely falls away when Staff’s methods used to compute clustered standard errors are

²⁰ See, e.g., *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009).

corrected, and pre-2013 pricing data are eliminated, AT&T would not oppose a compromise under which the Commission applies a reasonable competitive market test to DS1 and DS3 services. AT&T proposed such a test in its Comments, and that test has the twin virtues of being administrable and accurate. Indeed, we demonstrated that the test would designate as competitive only those census tracts where multiple facilities-based competitors are in position to compete for business at the vast majority of locations. If the Commission wishes to update its competitive market test for DS1 and DS3 services, it should adopt this test.

Third, there is no legal or policy basis for wholesale discounts on BDS prices. In addition to seeking indefensible adjustments to price cap mechanisms, a handful of CLECs ask for *additional* price breaks through mandated wholesale discounts. Only a handful of CLECs press for a wholesale discount – for all of its excesses, the Verizon/INCOMPAS “compromise” does not include any such provision, and Verizon opposes it.²¹ Those who do seek a mandated wholesale discount offer no legal or policy foundation for it. The Commission has long held that Sections 201 and 202 prohibit use restrictions and that section 251(c)(4) does not apply to predominantly wholesale services, such as the “Layer 2” Ethernet services for which CLECs now seek a wholesale discount.²² Nothing in the record supports a reversal of these longstanding

²¹ Comments of Verizon, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services; 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 Service*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 9-10 (June 28, 2016) (“Verizon 6/28 Comments”).

²² Indeed, as the Commission has recognized, a predominantly wholesale service would not have the sort of “avoided costs” that could form the basis for a wholesale discount in the provision of such services. First Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd. 15499, 15935, ¶ 874 (1996) (“*Local Competition Order*”). In all events, a section 251(c)(4) discount could only be established through the section 252 process of negotiations and state arbitrations, not by Commission mandate.

precedents. To the contrary, without any special wholesale discounts, non-ILEC competitors have won more than half of all BDS revenue, and they have deployed fiber virtually everywhere there is demand for BDS. In the Ethernet space, their success has been even more pronounced. In fact, the only support these CLECs can muster for their unlawful requests are recycled and already-refuted anecdotal claims of ostensible “price squeezes.” But apart from being wrong, these anecdotes prove nothing: a claim that a wholesale rate is *higher* than the retail rate for the same service may provide grounds for a section 202 complaint, but it does not establish a need for a rule mandating wholesale rates that are *lower* than corresponding retail rates.

Fourth, there is no support in the record for major X-Factor changes or for a one-time adjustment of price cap indices. As Drs. Meitzen and Schoech have explained, if the Commission were inclined to adopt a new productivity-based X-Factor, the best publicly available data – which are the Bureau of Labor Statistics official total factor productivity estimates for the communications industry – would support an X-Factor of no higher than 1.99 percent, if the Commission were to rely on the most recent updated data for 2005-2014.²³ The same BLS data also make clear that total factor productivity gains since 2005 have been roughly equal to inflation and thus no one-time price adjustment is warranted. Indeed, the Commission Staff’s new regression analyses dramatically confirm these points. The Commission Staff regressions for the first time separately break out the results by areas with Phase II, Phase I, and no pricing flexibility relief. Those regressions found no evidence that price cap LECs reduce

²³ Christensen Associates, “Reply Comments of Mark E. Meitzen & Philip E. Schoech,” *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 Cal 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, at 1-2 (filed Aug. 9, 2016) (“Christensen Reply Comments”).

prices in response to increases in competitive presence in Phase I areas, even though they have the same flexibility to do so in those areas as they do in Phase II areas. The only possible explanation is that price caps are already at or below competitive levels; even if the Commission were right that price cap LECs have market power, the regression results confirm that price caps constrain them from raising prices in locations with less competitive entry. The only competing X-Factor analysis in the record is Sprint's, which is based on productivity statistics sourced from a European Union research consortium, but those data are measures of value-added productivity that are not appropriate for estimating productivity adjustments for price caps, which regulate the total price of the service and thus require a gross output productivity measure.

In sum, if this is to be a “data-driven” proceeding, the Commission must follow the data and scale back its proposed framework of intrusive *ex ante* rate regulation. The risks of over-regulation are especially acute for Ethernet services, where the sudden imposition of unnecessary rate regulation on these rapidly growing services could introduce severe disincentives for broadband investment and do lasting harm to the IP transition.

I. THE RECORD EVIDENCE DOES NOT SUPPORT THE RADICAL NEW REGULATIONS FOR BDS PROPOSED IN THE NOTICE AND BY CLECs.

The record evidence – including the results of analyses of the 2013 data collection – overwhelmingly confirm that the marketplace for BDS is characterized by intense, growing, and nearly ubiquitous competition among multiple facilities-based providers.

The *Notice* acknowledges that any legitimate analysis of the BDS marketplace must account for facilities-based alternatives that are either in or near a location with BDS demand because BDS providers deploy networks in areas where there is demand for BDS and then

compete for customers within about a half mile of that demand.²⁴ Undisputed analyses of the 2013 data collection shows that, even as of 2013, virtually all (98.7 percent) of buildings with BDS demand were within a half mile of competitive facilities.²⁵ 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), and 90% were within about 1,107 feet (0.21 miles).²⁶ Most of the *demand* (measured by bandwidth) is also 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 And 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 In the years since 2013, competitors have continued to expand their networks. The special access data set itself shows that competitors experienced very substantial

²⁴ See, e.g., Notice ¶ 161; see also Comments of AT&T Inc., *Business Data Services in an Internet Protocol Environment; 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, 05-25, RM-10593, at 11-12 (June 28, 2016) ("AT&T 6/28 Comments"); Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, *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. 05-25, RM-10593, ¶ 43 (Apr. 14, 2016) ("Baker Decl."); Declaration of Mark Israel, Daniel Rubinfeld & Glenn Woroch ¶ 48 (Feb. 19, 2016) ("IRW 2/19 Decl."), attached as Attachment A to the Reply Comments of AT&T Inc., *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. 05-25, RM-10593 ("AT&T 2/19 Reply Comments"); Rysman White Paper at 11; IRW Second White Paper at 2; IRW Third White Paper at 2, 4.

²⁵ IRW Second Supp. Decl. ¶ 6.

²⁶ *Id.* ¶ 5.

²⁷ IRW Second White Paper at 5.

²⁸ *Id.*

growth even during 2013, and that this growth significantly outpaced that of ILECs.²⁹ Experts uniformly recognize that this growth has continued and, indeed, accelerated.³⁰

This intense competition is borne out by the regression analyses performed by Professor Rysman and Commission Staff. Those regressions show no evidence of market power for any Ethernet service or for any high band services (above 50 Mbps). And while they purport to find some evidence of market power for DS1 and DS3 services, the peer reviews and other economic analyses of those regressions confirm that these findings are overstated due to flaws in the data and the methods used for the regressions. As discussed below, when those items are fixed, the evidence of DS3 market power vanishes and the evidence of DS1 market power is *de minimis*, showing prices may be inflated by at most only about 3 percent in areas with no facilities based alternatives.

Based on these data-driven analyses, AT&T has supported a revised regulatory regime that would regulate BDS only in the areas not yet subject to proven (according to the 2013 data) facilities-based competition.³¹ By contrast, certain CLECs continue to ignore this evidence and argue for extensive and radical new regulation of virtually all BDS, including Ethernet, high band services (above 50 Mbps), and DS1 and DS3 services. As demonstrated below, these proposals have no support in the data, and could only hinder the already enormous investments, expansions, and innovation taking place in the BDS marketplace.

A. There Is No Record Support For Proposals To Regulate Ethernet Services.

The comments and data confirm that there is no legal or factual basis for the Commission to impose new *ex ante* rate regulations on Ethernet services. Rather the evidence demonstrates

²⁹ IRW First White Paper at 23-24.

³⁰ *See infra* at 19-21.

³¹ AT&T 6/28 Comments at 36-52.

that Ethernet services are subject to robust competition and that regulation of them is thus, not only unnecessary, but would thwart investment and innovation. Although, the Commission has proposed benchmarking in lieu of full blown *ex ante* rate regulation of Ethernet services, even such “lighter touch” regulatory measures are unnecessary and would likely be unworkable.³²

³² See, e.g., *id.* at 28-36; Joint Comments of CenturyLink, Inc., Consolidated Communications, Fairpoint Communications, Inc., and Frontier Communications Corp., *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 20 (June 28, 2016) (“Mid-Size 6/28 ILEC Comments”) (“The FNPRM’s proposal to subject Ethernet services to rate regulation ignores the realities of the BDS marketplace. Light-touch regulation over the past decade has fostered significant investment and declining prices in the Ethernet services market, both bellwethers of robust and effective competition.”); Comcast 6/28 Comments at 27-28 (“[T]here are several reason to be skeptical of the net benefits of imposing rate regulation to *any* extent in today’s BDS marketplace”); Comments of Cox Communications, Inc., *Business Data Services in an Internet Protocol Environment; Special Access for Price Cap Local Exchange Carriers*, WC Docket Nos. 16-143, 05-25, at 21 (June 28, 2016) (“Cox 6/28 Comments”) (“There is little question that some of the proposals in the *Further Notice*, including setting benchmarks to apply to all providers in ‘non-competitive’ markets, could have an adverse effect on investment in BDS”); Comments of the Fiber to the Home Council Americas on the *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 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, at 2 (June 28, 2016) (“Fiber to the Home Council 6/28 Comments”) (“The Council submits that the Commission should refrain from regulating the rates, terms, and conditions for high performance BDS offered by any provider over all-fiber networks.”); Comments of the Free State Foundation, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 2 (June 28, 2016) (“New regulation would deter competitive entry and investment in next-generation IP-based broadband services to the detriment of consumers.”); Comments of Hawaiian Telecom, Inc., *Business Data Services in an Internet Protocol Environment; Special Access for Price Cap Local Exchange Carriers*, WC Docket Nos. 16-143, 05-25, at 15 (June 28, 2016) (“Hawaiian Telecom 6/28 Comments”) (“The Commission proposes to set previous [sic] unregulated services, such as forborne Ethernet services, based on ‘benchmark prices.’ Hawaiian Telecom opposes any effort to price competitively provided IP-based services based on the price

1. The Evidence Confirms That There Is No Non-Arbitrary Basis On Which The Commission Could Regulate Ethernet Services.

Several commenters correctly point out that the Commission has never tried to reverse a grant of forbearance under Section 10 and re-impose regulation, and there are substantial questions as to whether the Commission even has authority to do so.³³ Whether or not that is the case, the Supreme Court has specifically held 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.”³⁴ No such showing could possibly be made here.

of another service.”) (footnote omitted); Comments of the National Cable & Telecommunications Association, *Business Data Services in an Internet Protocol Environment; Special Access for Price Cap Local Exchange Carriers*, WC Docket Nos. 16-143, 05-25, at 60 (June 28, 2016) (“NCTA 6/28 Comments”) (“There is no market failure for Ethernet services that justifies the imposition of an *ex ante* rate regulation or forced network sharing.”).

³³ See, e.g., AT&T 6/28 Comments at 30 (“The Commission has never purported to undo or re-impose regulation where there has been forbearance under Section 10 of the Communications Act.”); Mid-Size ILECs 6/28 Comments at 32-34; Hawaiian Telecom 6/28 Comments at 20; Comments of NASUCA and the Maryland People’s Counsel on Further Notice of Proposed Rulemaking for Business Data Services, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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, 15-247, 05-25, RM-10593, at 9 (June 28, 2016) (“Finally, a major part of the FCC’s proposals is the reversal of previous forbearance grants – along with some expanded forbearance. The statute does not contain an explicit provision for withdrawal of a previously-granted forbearance.”) (footnote omitted); see also 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).”).

³⁴ *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.”).

To begin with, by any reasonable standard, the Ethernet marketplace is far more competitive today than it was in 2007. Output is exploding, investment is surging, and prices are plummeting. These are all hallmarks of an intensely competitive marketplace, and they document the success, not failure, of the forbearance regime. For this reason alone, it would be arbitrary in the extreme for the Commission to reregulate Ethernet services.

The data collection only confirms that the Ethernet marketplace is intensely competitive. Indeed, Professor Rysman and Commission Staff conducted dozens of regressions examining pricing of high-bandwidth services (above 50 Mbps), including Ethernet services, and found no evidence of ILEC market power in those services.³⁵ And although neither Professor Rysman nor Commission Staff claim to have run regressions for Ethernet services below 50 Mbps, Drs. Israel, Rubinfeld, and Woroch took Professor Rysman’s regression models and ran them for those services, and the results were the same – no evidence of market power.³⁶ Thus, these regressions produce *zero* evidence of any market power in services above 50 Mbps and in any Ethernet service, regardless of bandwidth.

Even beyond the analyses of the 2013 data, the comments point to myriad third party data sources that confirm that the structure of the Ethernet marketplace ensures competition. There are dozens of non-ILEC providers of Ethernet services, and no provider has a port share that

³⁵ Rysman White Paper at 24 (“The fact that I do not detect an effect of competition for high bandwidth lines has an important implication for interpreting results.”); Commission Staff Response, Attachment 2, at 4 (“With respect to high bandwidth connections, the Rysman White Paper results appear to be much more of a true average of the three regulatory areas. While there are differences in the competitive effects between regulatory regimes, there is little indication of the presence of market power. Nearly all coefficients on competition are not statistically different from zero.”); *Notice* ¶ 244 (“The Rysman White Paper finds little statistical relationship between the presence of local fiber-based competition and lower incumbent LEC prices for BDS above 45 Mbps.”).

³⁶ IRW Second White Paper at 25-26.

exceeds one-fifth of the market.³⁷ Nine providers have port shares of four percent or more, including three CLECs, and three of the nation’s largest cable companies.³⁸ Other providers – *i.e.*, those with port shares under 4 percent – together have, in the aggregate, port share in excess of 20 percent.³⁹ According to a recent report by Ovum, Ltd. “North America remains the most dynamic Ethernet market [compared to its European and Latin American counterparts]” and the North America’s “open market has the greatest number of [competitive providers]” and “the greatest number of large-scale data center operators.”⁴⁰ The high number of facilities-based competitors and the low concentration confirm that the marketplace for Ethernet is and will continue to be highly competitive.

But the evidence of intense competition for Ethernet services does not stop there. Three hallmarks of competitive markets are falling prices, skyrocketing demand and output, and investment in infrastructure. All three of these trends are indisputably on display in today’s dynamic Ethernet marketplace.

Prices. Ethernet prices have fallen dramatically in recent years, and this trend is expected to continue. Even the Joint CLECs admit that ILECs prices “have declined since 2013 even in non-competitive areas.”⁴¹ Zayo describes “average annual price decreases between 2010 and

³⁷ See 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”).

³⁸ See *id.*

³⁹ See *id.*

⁴⁰ Ovum, “Ethernet Services Forecast Report: 2015-20,” at 16 (Sept. 28, 2015).

⁴¹ Comments of Birch, EarthLink, and Level 3, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier*

2015 for its GigE Full Rate (>1000 Mbps) and Fractional GigE (101-1001 Mbps) services of 4.9 percent and 10.1 percent, respectively.”⁴² Windstream likewise reports dramatic reductions in Ethernet prices.⁴³

They are not alone. Cable companies also report falling Ethernet prices. Comcast explains that the “high and increasing level of competition” in the BDS marketplace is having “a predictable effect on prices, which have been declining substantially for several years,”⁴⁴ and documents the substantial reductions in its rates for Ethernet services.⁴⁵ Charter Communications notes that additional investment in facilities-based infrastructure has “contributed to broadly declining prices for BDS.”⁴⁶ According to Cox, Ethernet prices have fallen “so precipitously that Cox is finding it harder to justify the costs of new fiber deployment.”⁴⁷ And ACA reports a 57% decrease in Ethernet pricing since 2011.⁴⁸

Rates for Internet Special Access Services, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 71 (June 28, 2016) (“Joint CLEC 6/28 Comments”).

⁴² *Id.* at 8-9.

⁴³ See Comments of Windstream Services, LLC on the Further Notice of Proposed Rulemaking, *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 Nos. 16-143, 05-25, RM-10593, at 52 (June 28, 2016) (“Windstream 6/28 Comments”).

⁴⁴ Comcast 6/28 Comments at 18.

⁴⁵ *Id.* at 18-19.

⁴⁶ Comments of Charter Communications, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 2, 7 (June 28, 2016).

⁴⁷ Cox 6/28 Comments at 2. Despite these comments, there is no sign of abatement in the expansion of Ethernet networks.

⁴⁸ Comments of the American Cable Association, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data*

Other commenters echo these findings. The Fiber to the Home Council discusses a report from Ovum reporting that “between 2013 and 2015, Ethernet prices on a global scale were cut in half.”⁴⁹ USTA reports that “prices for a range of business broadband and data services have been falling.”⁵⁰ And Anna-Maria Kovacs, from the Georgetown Center for Business and Public Policy, shows that the price of Ethernet access is expected “to fall by about 9% per year over the 2015 to 2018 period and the price of Ethernet WAN services by about 5% per year over that timeframe.”⁵¹

Demand and Output. As prices fall, demand and output for Ethernet services continue to skyrocket. INCOMPAS reports an “ever-increasing demand for Ethernet services,”⁵² while the

Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 36, fig. 3 (June 28, 2016) (“ACA 6/28 Comments”).

⁴⁹ Fiber to the Home Council 6/28 Comments at 7-8.

⁵⁰ Comments of the United States Telecom Association, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Service*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 14-15 (June 28, 2016) (citing Vertical Systems Group, @Ethernet Pricing, Overview (2016)) (“USTA 6/28 Comments”).

⁵¹ Anna-Maria Kovacs, *Business Broadband: Assessing the Case for Reregulation*, at 10 (Mar. 2016), available at <http://cbpp.georgetown.edu/sites/cbpp.georgetown.edu/files/Regulation%20in%20Financial%20Transaction%20Business%20Broadband%20Assessing%20the%20Case%20for%20Reregulation%20Kovacs%203.14.16.pdf>.

⁵² Comments of INCOMPAS, *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, at 4 (June 28, 2016) (“INCOMPAS 6/28 Comments”).

Competitive Carriers Association notes “the growing demand on wireless networks.”⁵³ TDS echoes these comments, noting that demand for bandwidth is “exploding,”⁵⁴ as does Comcast, which reports that demand for its business class data services has increased “substantially in recent years.”⁵⁵ Similarly, the Rural Wireless Association reports that with “consumer demand for mobile data services showing no signs of slowing down, mobile wireless providers are forced to deploy higher-capacity backhaul connections to their cell sites.”⁵⁶ And the Fiber to the Home Council explains that “demand for high performance services is growing substantially.”⁵⁷

Consistent with the universal recognition of rapidly growing demand, the *Notice* observes that “demand for high-bandwidth services [is] ris[ing]” and that “Ethernet services, especially over fiber, scale bandwidth to meet these demands more cost effectively than legacy TDM services.”⁵⁸ The *Notice* also acknowledges that “the demand for packet-based services will only

⁵³ Comments of Competitive Carriers Association, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 10 (June 28, 2016).

⁵⁴ Comments of TDS Metrocom, LLC, *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593, at 3 (June 28, 2016) (“TDS 6/28 Comments”).

⁵⁵ Comcast 6/28 Comments at 9.

⁵⁶ Comments of the Rural Wireless Association, Inc., *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593,, WC Docket No. 16-143, 15-243, 05-25, RM-10593, at 2 (June 28, 2016).

⁵⁷ Fiber to the Home 6/28 Comments at 9.

⁵⁸ *Notice* ¶ 80.

increase while legacy service sales shrink.”⁵⁹ And Vertical Systems Group has found that demand is solid as “[e]nterprises and SMBs will make purchase decisions to deploy hundreds of thousands of new Ethernet ports throughout the next several years, facilitated by a range of service options and competitive price points.”⁶⁰

Investment. Providers have responded to this growing demand by investing billions to deploy and expand Ethernet networks. The *Notice* itself cites Vertical Systems Group data that “Ethernet ports grew 26 percent in 2013, 24 percent in 2014, and by more than 20 percent in 2015.”⁶¹ The Comments document that Windstream had invested billions of dollars in its fiber network, TDS has invested over half a billion dollars for infrastructure, and half a billion dollars has been invested by XO.⁶² It shows that over a five year period Zayo, Level 3, Lightower, and TW Telecom invested approximately \$6 billion in fiber infrastructure.⁶³ Comcast reports investing “hundreds of millions of dollars in new fiber transmission facilities (and associated network equipment)” to better compete for BDS customers.⁶⁴ Cox describes investing billions of dollars.⁶⁵ Mediacom entered the market on a significant scale in 2011 and since that time “has deployed roughly 600,000 strand miles of carrier grade fiber backbone in its operating

⁵⁹ *Id.* ¶ 81.

⁶⁰ Vertical Systems Group, “One Million Carrier Ethernet Service Ports Projected in U.S. by 2018” (Sept. 25, 2014), <http://www.verticalsystems.com/vsgpr/one-million-carrier-ethernet-service-ports-projected-in-u-s-by-2018/>.

⁶¹ *Notice* ¶ 83.

⁶² *See* NCTA 6/28 Comments at 7.

⁶³ *Id.* at 8.

⁶⁴ Comcast 6/28 Comments at 8.

⁶⁵ Cox 6/28 Comments at 13.

territory.”⁶⁶ According to the American Cable Association, its smaller cable company members are making investments ranging from the tens of millions to \$300 million annually to deploy Ethernet facilities.⁶⁷ And the Fiber to the Home Council reports that the “number of fiber lit buildings” served by CLECs and cable providers increased “at an average rate of 14 percent between 2013 and 2015.”⁶⁸

These comments are consistent with AT&T’s experience. Outside of AT&T’s footprint, there has been an enormous increase in the number of buildings where AT&T can purchase Ethernet services from non-ILECs since 2013. CLECs and other providers seeking to sell Ethernet services to AT&T provide AT&T with lists of building they have “lit” with Ethernet services. These lists show that in 2013, AT&T could choose non-ILEC services in about [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] lit locations. Today, these lists include nearly [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] lit locations, a 20 fold increase.⁶⁹

As a result of this enormous increase in non-ILEC building coverage, the number of non-ILEC suppliers AT&T contracts with for enterprise Ethernet services has increased by five times since 2013, from [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] in 2013 to more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END

⁶⁶ Comments of Mediacom Communications Corp., *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 Nos. 16-143, 05-25, RM-10593, at 2 (June 28, 2016).

⁶⁷ ACA 6/28 Comments at 8.

⁶⁸ Fiber to the Home Council 6/28 Comments at 13.

⁶⁹ In addition, AT&T itself is investing more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] million dollars to expand its out-of-region Ethernet footprint.

HIGHLY CONFIDENTIAL] today. Currently, about **[BEGIN HIGHLY CONFIDENTIAL]**
[REDACTED] **[END HIGHLY CONFIDENTIAL]** of AT&T’s out-of region backhaul spend is for BDS
purchased from non-ILECs, which is a five-fold increase compared to 2013.

Prices paid by AT&T for Ethernet have plummeted as a result of this competition. The
prices that AT&T pays to ILECs for Ethernet services outside of its ILEC footprint have
decreased dramatically since 2013 for 10, 50, 100, and 1000 Mbps services, by an average of
more than **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED] **[END HIGHLY CONFIDENTIAL]**
percent. And AT&T’s rack rates for term plans have also decreased significantly over the last
three years **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED]
[REDACTED] **[END**
HIGHLY CONFIDENTIAL]

On this record there is no conceivable non-arbitrary basis for the Commission to
conclude that Ethernet services warrant reregulation. To the contrary, the evidence establishes
irrefutably that the marketplace is *far* more competitive now than it was then, and that the
Commission’s policy of forbearance has thus been an unqualified success in spurring lower
prices, higher demand, and more investment.

Only Sprint has filed a declaration attempting to show a lack of competition for Ethernet
services, but it actually shows the opposite – robust competition for Ethernet services.
Specifically, Sprint submitted a declaration by Dr. Chris Frentrup, Director and Senior
Economist for Sprint Nextel, Inc., that presents an analysis of Sprint’s “Network Vision” project,
“in which Sprint upgraded the backhaul to its entire network of towers.”⁷⁰

⁷⁰ Declaration of Chris Frentrup ¶ 2 (June 28, 2016) (“Frentrup Decl.”), attached as Exhibit B to
the Comments of Sprint Corp., *Business Data Services in an Internet Protocol Environment;*
Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff

Dr. Frentrup explains that “[s]tarting in late 2010, Sprint solicited bids to provide Ethernet backhaul to its more than 38,000 cell sites”⁷¹ as part of a project called “Network Vision.”⁷² The response to these bids confirms that the marketplace for services of 50 Mbps and above was highly competitive even in the 2010-2012 time frame during which these bids were solicited. Sprint received bids from more than 70 *different companies*, including ILECs, CLECs, and cable companies.⁷³ Moreover, Sprint received bids for [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of its cell sites, and it received at least two bids for [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of them, and at least three bids for about [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of them.⁷⁴ In other words, Sprint

Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593 (June 28, 2016) (“Sprint 6/28 Comments”).

⁷¹ Frentrup Decl. ¶ 4.

⁷² *Id.* Sprint itself identified potential bidders and provided them with the location of its cell sites. *Id.* ¶ 5. “Sprint specified that Ethernet service with a minimum capacity of 50 Mbps was required” and Sprint “required all connections to be ‘on-net’, *i.e.*, services needed to be provided over the bidder’s own facilities rather than over facilities purchased from other carriers.” *Id.* In addition, Sprint allowed only monthly recurring charges, no non-recurring charges were allowed. *Id.* Sprint also expressed a preference for seven-year terms, but entertained proposals with varying term lengths. *Id.*

⁷³ *Id.* ¶ 6.

⁷⁴ *Id.* The Frentrup Decl. reports metrics for all cell sites for which it sought bids. But Sprint did not receive bids for [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of cell sites. Frentrup Decl. ¶ 7. Sprint reports that it received at least two bids for [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of its cell sites, which means that it received at least two bids for about [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of the cell sites for which it received any bid at all. Likewise, Sprint reports that it received at least three bids for [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of sites, which means that it received at least three bids for about half of the cell sites for which it received any bid at all.

received multiple bids for the vast majority of the more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] cell sites spread across the U.S. for which it received any bid. Moreover, although Dr. Frentrup does not disclose the number, he states that non-ILECs accounted for a portion of the small number of cell sites for which Sprint received only a single bid.⁷⁵ Furthermore, Dr. Frentrup points out even for locations for which it received no bids, it was still able to use a range of BDS services, including “microwave backhaul.”⁷⁶ These metrics are further evidence of a robustly competitive Ethernet marketplace. That these data are from 2010-2012 only makes them more so.

Sprint tries to turn this wine to vinegar by presenting regressions purporting to show that the bids it received were lower for cell sites where there were more bidders. But Sprint’s regressions show no such thing. As explained by Drs. Israel, Rubinfeld, and Woroch, “it is impossible to draw any useful conclusions from these [regressions].”⁷⁷ First, it is impossible to “validate these regression results because Dr. Frentrup did not disclose the underlying data used in the regressions, nor did he disclose the methods used for the regressions.”⁷⁸ Indeed, “[i]t is not even clear how he determined whether the results are statistically significant”; “[t]here is no indication, for example, that he used clustered standard errors as recommended by the peer reviews of Professor Rysman’s paper.”⁷⁹ Thus, “[a]s a matter of standard professional practice, results that are not fully documented and thus cannot be scrutinized and checked over by third

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ IRW Third White Paper at 32.

⁷⁸ *Id.*

⁷⁹ *Id.*

parties should be given no credibility.”⁸⁰ Second, “interpreting regression results of bids in an auction requires substantial care” because basic auction theory teaches that “*any* auction” of this type will have lower prices with more bidders because there is a higher likelihood that one of the bidders will have lower costs.⁸¹

Third, and more generally, it does not appear that Dr. Frentrup has “controlled for endogenous factors that affect both bid levels and the number of bidders.”⁸² As explained above, no conclusions about causal relationships between prices and the number of competitors can be determined by running simple regressions. Rather, it is necessary to filter out other determinants of the observed relationship. For example, areas with favorable cost conditions are likely to have both more competitors and lower bids, and thus any conclusion that the number of competitors *caused* those lower bids would be unfounded. As explained by Drs. Israel, Rubinfeld, and Woroch, “[b]ecause Sprint’s analyses does not account for this ‘endogeneity’ problem, failing to even include any fixed effects (as Professor Rysman has done), the regression results provide no support for the conclusion that lower Ethernet prices are caused by a larger number of competitors.”⁸³

Windstream’s attempts to show market power in Ethernet services fare no better. Windstream attempts to rely on snippets from a study that BT Americas placed in the record last February that has been thoroughly debunked as a basis for regulating Ethernet services.⁸⁴ This

⁸⁰ *Id.*

⁸¹ *Id.*

⁸² *Id.*

⁸³ *Id.* at 32-33.

⁸⁴ Windstream 6/28 Comments at 3, 48-49, 52. *See* WIK-Consult, “Ethernet leased lines: An international benchmark,” attached to Reply Comments of BT Americas, *Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform*

study was conducted by a European telecom consultancy called WIK, which in turn used 2013 data reported by a separate consulting company called Ovum. The WIK study, relying on 2013 data from Ovum, purports to show that, compared to European countries where Ethernet prices are regulated, U.S. Ethernet prices are higher and U.S. Ethernet uptake are lower. But in 2015, Ovum updated the data set relied upon in the WIK study, and these updates show that U.S. prices have dropped substantially since 2013 due to intense competition, with U.S. prices quickly falling below those in Europe, and U.S. Ethernet uptake on par with that in Europe.⁸⁵ In other words, the updated Ovum data show that the *absence* of Ethernet regulation in the U.S. has resulted in more rapid declines in, and overall lower prices than, countries that have chosen to regulate Ethernet prices.⁸⁶ According to Ovum’s 2015 report, “North America remains the most dynamic Ethernet market,” describing it as “an open market” with “the greatest number of competitors.”⁸⁷ Thus, when Windstream argues that the WIK study shows the U.S. lagging behind its European counterparts and that the WIK study shows that regulating Ethernet can

Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, WC Docket No. 05-25, RM-10593 (Feb. 19, 2016).

⁸⁵ See Letter from Keith Krom (AT&T) to Marlene H. Dortch (FCC), *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. 05-25, RM-10593, at 1 (Mar. 29, 2016) (“AT&T 3/29 Letter”).

⁸⁶ *Id.* at 2-3.

⁸⁷ Ovum, “Ethernet Services Forecast Report: 2015-2020” (Sept. 28, 2015) and accompanying spreadsheet. The WIK study also compared U.S. “rack rates” to the “rack rates” in other countries. But this comparison is apples-to-oranges. The “rack rates” for the European countries in WIK’s comparison are the regulated rates from which providers generally cannot deviate. There is no analog to such rates in the U.S. Instead, the WIK Study incorrectly assumes that Ethernet prices listed in “service guides” by a few U.S. companies are the U.S. analog to European rack rates. However, as the WIK study acknowledges, the actual rates paid by U.S. customers are generally negotiated at discounted levels dramatically below those in the service guides. See AT&T 3/29 Letter at 4.

produce substantial benefits, it is relying on a fatally flawed study that is refuted by more current data.

2. The Comments Confirm that the Benchmarking And Other Proposal To Regulate Ethernet Are Unworkable And Would Undermine Investment, Innovation, and Competition.

There is broad-based concern in the comments about the Commission’s novel “benchmarking” proposal for regulating Ethernet services. First, although a “benchmark” price that functioned as a safe harbor might be less rigid or burdensome than the classic price cap regime, there is no basis in the record for *any* form of rate regulation in this space. Moreover, it is unrealistic to presume that the Commission’s proposed benchmarking scheme would be anything but intrusive.⁸⁸ The Commission should be well aware that, even in highly competitive markets, carriers will try to take maximum advantage of any regulatory angle that is available to them. Thus, even if “benchmark” rates are not binding in and of themselves, they will become the focal point of litigation, and every attempt will be made to turn them into *de facto* rate ceilings. In short, Commission intervention in the Ethernet space, even through what purports to be a light touch regime, is both unnecessary and counterproductive.

The risks of a benchmarking regime are magnified by the difficulty of fashioning such a regime. The proposals thus far range from benchmarking Ethernet prices to TDM-based services to benchmarking low-band Ethernet prices to high-band Ethernet prices, in all cases using an arbitrary “bandwidth-to-rate conversion” scheme that essentially assumes prices should be proportional to bit rates. There is no record evidence, however, that Ethernet is or should be priced linearly to bandwidth. And even if there were evidence of such linear pricing today, there

⁸⁸ Verizon’s suggestion (*see* Verizon 6/28 Comments at 16) that a “light touch” benchmark scheme would be “less burdensome” than the “dominant-carrier regime it replaces” has lost sight of reality; the benchmarks would replace *forbearance*, not dominant carrier regulation.

is no reason to freeze that pricing model in place. The Ethernet marketplace is highly dynamic, with many providers attempting to use different facilities to offer Ethernet services and experimenting with different qualities of services (including offering a wide range of service level guarantees). Imposing a linear pricing model on this dynamic space that effectively treats Ethernet service as a “dumb pipe” will only thwart innovation and prevent providers from tailoring their offerings to the specific demands of the marketplace.

Nor is there reason to believe that benchmarks would result in more “accurate” prices than what the parties can freely negotiate in the marketplace. Commenters are especially skeptical of the Commission’s ability to set appropriate Ethernet benchmark rates by applying some sort of bit-rate conversion factor to TDM rates. Even Verizon – one of the sponsors of the framework the Commission is proposing to implement – notes that TDM services come in two main increments (1.5 Mbps DS1s and 45 Mbps DS3s), which are not “comparable to any of the primary Ethernet services,”⁸⁹ and thus it is far from obvious exactly how the Commission could fairly convert these rates for legacy TDM to “correct” rates for Ethernet.⁹⁰ Similarly, Level 3 explains that it is “unlikely” the Commission could feasibly assign prices that would adequately account for “each capacity, each service quality level, each term plan, and possibly each different relevant geographic area.”⁹¹ The devil is always in the details of such proposals, but as AT&T previously explained, there would be numerous difficulties in designing such a conversion factor that the *Notice* does not acknowledge.⁹²

⁸⁹ Verizon 6/28 Comments at 21.

⁹⁰ *See also* Joint CLEC 6/28 Comments at 66-68 (noting implementation issues raised by the TDM benchmarking approach).

⁹¹ *Id.* at 67.

⁹² AT&T 6/28 Comments at 56-57.

The CLECs, of course, have ulterior motives for voicing skepticism about the feasibility of benchmarking. Ignoring the complete lack of evidence of any market failure for Ethernet services, they jump the shark with proposals for full-blown rate regulation and rate reduction proposals aimed solely at incumbent LECs. For example, Level 3 – the second largest Ethernet provider – argues that the Commission should re-impose tariffing and adopt price cap regulation for Ethernet services, but only for the “leading provider” of BDS – which, according to Level 3, would always be the incumbent LEC.⁹³ Level 3 also argues that the Commission should set the price caps to impose massive price reductions on the ILECs (although Level 3 argues without a trace of irony that the Commission should not use the 2013 rates in the data collection because Ethernet rates have been substantially reduced in the interim).⁹⁴ No less audacious, Windstream urges the Commission to use forward-looking cost studies (such as the Connect America Cost Model) to determine benchmark pricing for the “market leader” – which, again, would be the incumbent LEC.⁹⁵ For the reasons discussed above, there is no record evidence to support these requests; the data as to market structure and market performance, as well as the regression analyses, all show that ILECs do not possess market power in the Ethernet space. And adoption of these proposals would only stifle broadband investment.⁹⁶

Finally, the Commission should reject Verizon’s proposal to adopt a rule permitting customers to pay the benchmark rate during the pendency of any challenge to a carrier’s Ethernet

⁹³ Joint CLEC 6/28 Comments at 58-76.

⁹⁴ *Id.* at 70-71.

⁹⁵ Windstream 6/28 Comments at 42-43.

⁹⁶ Sprint makes a similar proposal, arguing that “the safe harbor prices should be initialized by applying a one-time 20 percent reduction to 2016 rates in non-competitive areas” with “annual reductions of 4.4 percent going forward,” although as a wireless carrier and not a CLEC, Sprint would then apply the resulting benchmark rates to all BDS carriers. Sprint 6/28 Comments at 65-66.

rates. Any such rule would improperly assume the validity of the benchmark rate before the Commission could even adjudicate the matter, and would encourage CLECs to file endless frivolous lawsuits for the purpose of securing the interim benchmark rate while their cases were pending. Moreover, the Commission lacks authority under Section 205 to order an interim prescription and force the carrier to charge a different rate during the pendency of a complaint,⁹⁷ and it cannot be the case that *forbearance* from Section 205 (and the rest of the tariffing regime) could give the Commission greater authority to dictate what rate a carrier may charge than it could under the tariffing regime.

B. The Record Evidence Confirms That There Is No Basis For Radical New Regulation For DS1 and DS3 Services.

The *Notice* relied largely on regressions performed by Professor Rysman as a basis for the proposed regulations of DS1 and DS3 services. However, the peer reviews and submission by other economists demonstrate that these regressions were flawed, both due to methodological flaws and intractable problems with the data. In response, the Commission Staff conducted dozens of new regressions, which purport to fix some, but not all, of these flaws. As demonstrated below, these new regressions fail to demonstrate market power for DS3 services, and indicate only *de minimis* market power for DS1 services. Moreover, these regressions continue to contain myriad flaws – both in data and methodology – that tend to overstate the market power indicators.

⁹⁷ See *AT&T v. FCC*, 449 F.2d 439, 451 (2d Cir. 1971) (striking down interim prescription); see also *AT&T v. FCC*, 487 F.2d 865, 872-80 (2d Cir. 1973); *Sw. Bell Corp. v. FCC*, 43 F.3d 1515, 1519 (D.C. Cir. 1995).

1. The Regressions Do Not Establish Substantial Market Power For DS1 Or DS3 Services.

Notwithstanding that competitive facilities are nearly ubiquitous and that competitors have been extremely successful, the CLECs and Commission Staff purport to find evidence of ILEC market power for DS1 and DS3 services in regressions conducted by Professor Rysman and in the revised versions of those regressions performed by Commission Staff in response to the peer review criticisms of Professor Rysman’s analyses. In fact, even if the regressions were accurate (they are not), they do not establish that ILECs exercise market power, and certainly not sufficient market power to justify the extensive new regulations proposed in the *Notice*. To conclude that these regressions provide “consistent” and “robust” evidence of market power, the Commission would have to arbitrarily reject results that do not support a finding of market power, while crediting only the few, less robust results that do. But any decision based on these sorts of “data mining” (rather than “data driven”) results-oriented approach would be a manifest violation of the APA, and could not survive judicial review.⁹⁸

The DS1 Regressions. The *Notice* relied on the regression results reported by Professor Rysman in Tables 14-16 as evidence of market power for DS1 services. But as discussed below, the peer reviews of his analyses found that these regressions overstated the magnitude and statistical significance of the results due to multiple data and methodological flaws. One of the issues raised by the peer reviews that the Commission Staff sought to address is the method for computing the statistical significance (Professor Rysman used “robust” standard errors rather

⁹⁸ See, e.g., *Am. Radio Relay League, Inc. v. FCC*, 524 F.3d 227, 237 (D.C. Cir. 2008) (“[T]here is no APA precedent allowing an agency to cherry-pick a study on which it has chosen to rely in part.”); see also *Kenty Cnty. v. EPA*, 963 F.2d 391, 396 (D.C. Cir. 1992) (arbitrary and capricious to rely on a single outside memorandum and not review other files).

than “clustered” standard errors). The Commission Staff therefore re-ran Professor Rysman’s regressions using clustered standard errors and reported the results in Tables 14.a-16.a.⁹⁹

The new regression results show no consistent evidence of ILEC market power. The Commission Staff correctly notes that Tables 14.a and 15.a contain statistically significant results indicating that ILEC DS1 prices are about 3.2% lower in areas where there is at least one other provider serving a building in the same census block. But the regressions reported in Tables 16.a find *no statistically significant* evidence that ILEC prices are lower when there is at least one other provider serving a building in the same block.¹⁰⁰ Thus, the regressions at best produce inconclusive results.

The Commission Staff responds by declaring, with no supporting evidence or analysis, that the Table 16.a results can be ignored because they “push[] the data far enough that we cannot reliably estimate the effect of competition.”¹⁰¹ The Commission Staff is incorrect: as Drs. Israel, Rubinfeld, and Woroch explain, Table 16.a actually produces the more reliable result compared to Tables 14.a or 15.a, because it is the more precise regression.¹⁰² The Commission is not free under the APA to arbitrarily pick results that support its pre-determined conclusions and ignore more robust ones that do not.

Further, the results for Tables 14.a and 15.a do not establish a level of market power that could justify the new regulations proposed in the *Notice*. To the contrary these regressions show that ILEC prices are at most only about 3.2 percent above competitive levels in areas without at

⁹⁹ Commission Staff Response, Attachment 1.

¹⁰⁰ The Commission Staff’s regression that separately examines price cap, Phase I and Phase II areas found similar contradictions for Phase II areas. *See id.*, Attachment 2, tbls. 14.a-19.c.

¹⁰¹ *Id.*, Attachment 1 at 2.

¹⁰² IRW Third White Paper at 23-24.

least one other provider. Professor Rysman himself emphasized that this effect is “not especially large by the standards of competition analysis.”¹⁰³ Indeed, 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). Consequently, these regressions fail to document any problem that warrants regulatory intervention.

The Commission Staff’s own statements elsewhere confirm that these DS1 regression results are not competitively significant. When examining its regression results for price cap areas, the Commission Staff’s regression produced statistically significant results indicating that ILEC prices are from 1.4% to 2.7% lower in areas with competitive entry. To downplay the fact that such results raise serious concerns about the legitimacy of the regressions (because, as explained below, the price cap rules constrain ILECs’ ability to adjust prices in response to competition in price cap areas) the Commission dismisses these results on the grounds that these differences provide “little evidence that the presence of competition affects ILEC prices in price cap regions.”¹⁰⁴ Yet, the Commission Staff purports to find evidence that the presence of competition affects ILEC prices in other (non-price cap) areas when the impact on ILEC prices range are only about 3.2%.¹⁰⁵ The Commission Staff provides no explanation as to why a 2.7% price effect is not evidence that the presence of competition affects ILEC prices, whereas a 3.2% price effect is.

Regulatory intervention to remedy a purported 3.2% price differential would be particularly inappropriate because of the *costs* imposed by such intervention. As the Supreme

¹⁰³ Rysman White Paper at 21-22.

¹⁰⁴ Commission Staff Response, Attachment 2, at 1.

¹⁰⁵ *See, e.g., id.*, Attachments 1-2.

Court recently explained in *Michigan v. EPA*,¹⁰⁶ 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.”¹⁰⁷ Here, the costs and burdens of the Commission’s proposed regime could be enormous and would easily offset any gains from regulations that reduce ILEC prices by only 3.2 percent in the few areas where competitors have not yet deployed facilities. 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 affect 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 substantial time to accomplish.

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.¹⁰⁸ 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 DS_n 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

¹⁰⁶ 135 S. Ct. 2699 (2015).

¹⁰⁷ *Id.* at 2707 (emphasis in original); *see also id.* (“[n]o regulation is ‘appropriate’ if it does significantly more harm than good”).

¹⁰⁸ *See* IRW Second White Paper at 21.

process of retiring. Under any reasonable calculus, these concrete and substantial harms outweigh the dubious benefits of reregulation of BDS.

In an apparent effort to find some regression results to support a finding of market power, the Commission Staff ran dozens of other regressions as well, but found only the same mixed and *de minimis* results for DS1 services. For example, the Commission Staff conducted regressions separately for price cap (no relief), Phase I, and Phase II areas.¹⁰⁹ But again the regressions produced contradictory results and only further confirm that these regressions cannot be relied upon as evidence of ILEC market power. For example, for Phase II areas, the regression results reported in Tables 14.a and 15.a produce statistically significant indications of ILEC market power, whereas Table 16.a – which, as with the original regressions, is the more accurate regression – produced no statistically significant results.

More fundamentally, these revised regressions exhibit the kind of nonsensical results that confirm that the regressions are clearly overstating the extent to which ILECs can exercise market power. For example, if these regressions were actually measuring ILEC pricing responses to competitive entry, there should be no statistically significant relationship between ILEC prices and competitive conditions in price cap areas (*i.e.*, areas with no Phase I or Phase II relief) because ILECs lack sufficient flexibility under the price cap rules to substantially increase or decrease prices in response to competition in those areas. But, as noted, the Commission Staff's regressions purport to show statistically significant results indicating that ILEC prices are lower in areas with more competitors. Because this result cannot be attributed to ILECs increasing or decreasing prices in response to competitive entry, these results confirm that the regression results are capturing other, unobserved, factors producing a correlation between ILEC

¹⁰⁹ Commission Staff Response, Attachment 2.

prices and competitive conditions that have nothing to do with market power, and that therefore *overstate* the extent to which these regressions indicate market power.¹¹⁰

As discussed below, the peer reviewers and other economists have identified multiple underlying problems with the methods and data used in these regressions that could account for these anomalous results. But whatever the reason for these results, they confirm there is no legitimate basis for interpreting *any* of the regression results as being indicative of market power. Indeed, given that it is undeniably certain that the statistically significant results for price cap areas cannot legitimately be interpreted as ILEC market power, it follows that other statistically significant results for Phase I and Phase II areas are likely also “false positives” that cannot be taken as evidence of ILEC market power.¹¹¹

The DS3 Regressions. The *Notice* also relied on the regression results reported by Professor Rysman in Tables 14-16 as evidence of market power for DS3 services. But again, when the Commission revised the regressions to compute statistical significance using “clustered” standard errors, the regressions produced the same inconsistent results as observed for DS1 services: Tables 14.a and 15.a contain statistically significant results indicating that ILEC DS3 prices are lower in areas where there is at least one other provider serving a building in the same census block, but the regressions reported in Tables 16.a find *no statistically significant* evidence that ILEC prices are lower when there is at least one other provider serving a building in the same block. Thus, as with the DS1 regressions, the DS3 the regressions produce no consistent evidence of market power.

¹¹⁰ See IRW Third White Paper at 20.

¹¹¹ *Id.* at 20-23.

Moreover, as explained by Drs. Israel, Rubinfeld and Woroch, the Commission Staff computed the clustered standard errors incorrectly, and when done properly, virtually all of the regression results for DS3 services become statistically insignificant – even those in Tables 14.a and 15.a.¹¹² They explain that the key to correctly computing a clustered standard error is identifying reasonably sized geographic areas in which prices and competitive conditions for BDS are likely to be significantly correlated.¹¹³ The Commission Staff chose to cluster at the census block level. But census blocks are too small an area about which to cluster for this purpose (and, indeed, Professor Sweeting also raised this criticism in his review of the Commission Staff’s analyses).¹¹⁴ Indeed, as the Commission Staff concedes, more than two-thirds of census blocks contain only a *single* BDS connection, so it is barely “clustering” at all. As a result, clustering by census block fails to properly aggregate buildings where pricing and competitive conditions will be highly correlated, and it fails to cluster at all for two thirds of the connections.¹¹⁵

Drs. Israel, Rubinfeld and Woroch show that clustering at the census *tract* level is more accurate than clustering at the census *block* level, because they find substantial correlation among prices and competitors at the census tract level.¹¹⁶ And when census tracts are used to compute the standard errors, virtually all of the results for DS3 services in the original regressions performed by Professor Rysman become statistically insignificant.¹¹⁷

¹¹² *Id.* at 24-25.

¹¹³ *Id.*

¹¹⁴ Sweeting First Review ¶ 7.

¹¹⁵ IRW Third White Paper at 24-25.

¹¹⁶ *Id.*

¹¹⁷ *Id.*

Number Of Competitors Needed To Produce Competitive Outcomes. The economic testimony demonstrates that two providers (*e.g.*, an ILEC plus a CLEC) are sufficient to ensure reasonably, competitive outcomes in the BDS marketplace.¹¹⁸ This testimony is consistent with years of Commission and D.C. Circuit precedent.¹¹⁹ Nonetheless, the original regressions produced by Professor Rysman purported to show that ILEC prices were increasingly lower as more competitors entered the marketplace, which the *Notice* suggests may be evidence that more than one competitor in addition to the ILEC is needed to obtain reasonably competitive outcomes. These regression results were reported by Professor Rysman in Table 19. Once again, however, when the Commission applied clustered standard errors to the regressions – as suggested by the peer reviews and other economists – the revised regressions showed no consistent evidence that more than one competitor (in addition to the ILEC) produces more competitive outcomes.

For DS3 services, the Commission Staff’s analyses shows no statistically significant effect on ILEC prices in Table 19 when there is one competitor, a 15.4 percent impact on ILEC prices if there are two or three competitors, and then no competitive effect when there are four or more competitors – a pattern that makes no economic sense.¹²⁰ Moreover, as noted, the Commission Staff’s method of computing the clustered standard error is wrong. When it is corrected, there are no statistically significant results for DS3 services in Table 19.¹²¹ Indeed,

¹¹⁸ *See, e.g., id.* at 2.

¹¹⁹ *See, e.g., WorldCom*, 238 F.3d at 458-59 (“the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed”); *Pricing Flexibility Order* ¶ 80 (same); *Unbundled Access Order* ¶ 63 (recognizing that “facilities-based competition” is the “most effective discipline to anticompetitive price squeezes”).

¹²⁰ IRW Third White Paper at 20, 24; Commission Staff Response, Attachment 1.

¹²¹ IRW Third White Paper at 24-25.

when the Commission Staff focused on only Phase II areas, where ILECs are unconstrained by price cap regulation in their ability to raise and lower prices in response to competition, it found no statistically significant results at all for DS3 services in Table 19.¹²²

For DS1 services, the Commission Staff results are schizophrenic. Correcting the original Rysman regressions to account for clustered standard errors still produces statistically significant results for Table 19. But, when the Commission runs the regressions separately for Phase II areas, it finds contradictory results. As explained by Drs. Israel, Rubinfeld, and Woroch, there is no legitimate economic justification for such results.¹²³ The only explanation is that the regression results are wrong, due to bad data, an invalid methodology, and/or some other unobserved factor, unrelated to the exercise of market power.¹²⁴

The Commission Staff is therefore forced to dismiss its own regressions, claiming that “we do not believe that this result is definitive, but simply asks more of the data than it can provide.”¹²⁵ That has things backwards: the Commission Staff’s regressions are the *corrected* ones. There is no legitimate basis for the Commission to continue to credit Professor Rysman’s original results – which, as discussed below, the peer reviews found to be flawed – rather than crediting the revised regressions, which show no evidence of market power. In all events, as explained above, the Commission is not free to arbitrarily pick the results that support its preferred outcome and dismiss those that do not.

¹²² Commission Staff Response, Attachment 2, tbl. 19.c.

¹²³ IRW Third White Paper at 24.

¹²⁴ *See id.*

¹²⁵ Commission Staff Response, Attachment 1, at 2.

2. Even If The Results Of The Commission Staff’s Regressions Established Non-De Minimis Market Power, The Regressions Overstate The Market Power Indicators And Are Overall Fundamentally Flawed.

Even if the Commission could cherry-pick the few results from the regressions that support an ILEC market power theory, there is no legitimate basis for the Commission to assume that those results are accurate. The peer reviews and other economists documented numerous methodological and data flaws in Professor Rysman’s original regressions that could not be corrected, and that the Commission Staff’s revised regressions do not purport to correct. Many of these errors overstate both the magnitude and statistical significance of the results. Thus, even where the Commission finds results that support a finding of ILEC market power, those results cannot be relied upon. As Professor Sweeting concludes, “partly because of the limitations of the data available, the results should be interpreted with caution (as Dr. Rysman himself suggests in his conclusions).”¹²⁶

Endogeneity (Correlation/Causation Problem). The reviewers and other economists recognize that Professor Rysman’s original regressions suffer from a serious “endogeneity” problem. Professor Rysman’s paper attempts to test whether ILECs have market power for DS1 and DS3 services using regressions that compare ILEC prices in areas with differing numbers of competitors.¹²⁷ The theory behind this comparison is that if ILEC prices are lower in areas with more competitive entry, then ILECs are exercising market power.¹²⁸ But this test is legitimate only if one can be sure that competitive entry is *causing* the observed lower ILEC prices. If the ILECs and competitors are both reacting to other underlying economic conditions such as lower

¹²⁶ Sweeting First Review ¶ 2. *See also* Rysman White Paper at 20-22, 25.

¹²⁷ Rysman White Paper at 2.

¹²⁸ *Id.*

costs or higher revenue opportunities – *i.e.*, if lower ILEC prices are merely correlated with competitive entry – then no inference of market power can be drawn.

Put another way, to establish market power, Professor Rysman must show that, *holding all other economic conditions constant*, adding an additional competitor *causes* lower ILEC prices. If the regression model does not in fact hold economic conditions constant, then there is an “endogeneity” problem and the approach is not a valid test of market power.¹²⁹

Professor Rysman himself acknowledged this issue as a “major concern” with his model:

A major concern is that locations differ in important and unobservable ways. For instance, locations may differ in how costly they are to serve with BDS. Thus, low cost areas might see low prices and high competition independent of any causal effect of competition on price. Locations also differ in their regulatory status, such as whether they are subject to price flex regulation, and locations differ to the extent they face competition from outside the BDS market.”¹³⁰

Professor Rysman attempted to partially address this concern by applying an econometric technique called “fixed effects.” But as Drs. Israel, Rubinfeld, and Woroch have explained, fixed effects techniques cannot address the problem here, especially if there is variation in economic conditions within census tracts, because the fixed effects approach used by Professor Rysman can address endogeneity only between census tracts, not within them.¹³¹ Professor Rysman had the same concern:

My approach is problematic to the extent that unobserved effects differ across census blocks within the same census tract. For instance, it might be the unobserved costs of providing service varies substantially even within census tracts.¹³²

¹²⁹ See IRW Second White Paper at 9-17; IRW Third White Paper at 16-19.

¹³⁰ Rysman White Paper at 20.

¹³¹ IRW Second White Paper at 14-15; IRW Third White Paper at 16-19.

¹³² Rysman White Paper at 20.

Drs. Israel, Rubinfeld, and Woroch have shown that there is indeed substantial variation in economic conditions between census blocks.¹³³ The peer reviewers agree that Professor Rysman’s analyses, even after applying the fixed effects techniques, continue to raise substantial endogeneity concerns. For example, Professor Valletti explained that:

[T]he question remains whether it is still possible that unobserved factors that can affect prices (particularly demand and supply characteristics) different within the census tract, and could drive the entry of CPs.¹³⁴

Likewise, Professor Sweeting explained:

Given that the analysis uses cross-sectional data it is also necessary to make the assumption that entry of competitors is not more likely to happen where ILEC prices for BDS services would naturally be low, which might happen if there are areas where customers are more likely to purchase a wide range of ILEC products of which BDS services are simply a small part.¹³⁵

The revised regressions performed by Commission Staff do not attempt to address this endogeneity issue. Thus, it is impossible to determine whether the observed pricing differences in Professor Rysman’s original regressions, or the Commission’s revised regressions, actually suggest market power or are merely responses to other economic conditions that drive the actions of all competitors. Indeed, in many cases, the regression results will be capturing instances where only lower costs have resulted in both lower ILEC prices and greater competitive entry, thus creating false positives for market power, and even where the findings of market power are legitimate, the magnitude of the market power may be dramatically overstated because the regressions are also capturing endogenous effects that are not related to market power. Thus, the

¹³³ See IRW Third White Paper at 18-19.

¹³⁴ Valletti First Review at 6.

¹³⁵ Sweeting First Review ¶ 7. See also *id.* ¶ 19 (“using fixed effects and trying multiple specifications . . . does not remove the [endogeneity] problem entirely”).

regression results cannot reasonably be used to conclude that ILECs exercise market power for DS1 or DS3 services.

Flawed Pricing Data. Accurate pricing data is critical to producing valid regression results, because the purpose of the regressions is to compare ILEC prices across areas with varying levels of competitive entry. The peer reviewers and other economists identified several serious flaws in the pricing data that affected the regression results.

First, the regressions rely on substantial amounts of pricing data from the wrong year. The purpose of these regressions is to measure the extent to which different competitive conditions cause observed variations in price. Many of the prices in the data collection, however, were negotiated in long-term contracts *prior* to 2013, and thus obviously could not have been caused by competitive conditions in 2013.¹³⁶ Professor Mayo confirmed that a large portion of the pricing data in Professor Rysman’s regressions were in fact established prior to 2013, and Professors Israel, Rubinfeld, and Woroch show that the Commission Staff Papers use the same flawed pricing data as Professor Rysman.¹³⁷ Thus, any relationship between the prices used in the regressions and competitive conditions cannot be a causal relationship, and thus cannot legitimately be relied upon as evidence of market power.¹³⁸

Professor Mayo confirms that the inclusion of pre-2013 prices in the regressions substantially biased the results.¹³⁹ He shows that when these older prices are excluded from the

¹³⁶ See Mayo Decl. ¶ 71 (“It is impossible for *Competitive Presence* – observed in 2013 – to cause prices that were set in earlier years!”); Sweeting First Review ¶ 9 (“[T]he fact that there is only one year of data may create some additional issues. For example, many of the contracts observed are likely to have been negotiated some time prior to 2013, when local competition may have been different”); see also IRW Third White Paper at 12-13.

¹³⁷ See Mayo Decl. ¶ 71; IRW Third White Paper at 12-13.

¹³⁸ See Mayo Decl. ¶ 71; see also IRW Third White Paper at 12-13.

¹³⁹ See Mayo Decl. ¶¶ 72-78.

regressions, the regressions generally produce statistically significant *positive* relationships between ILEC prices and competitive entry for DS1 prices – *i.e.*, ILEC DS1 prices go *up* where there are more competitors – and he found that DS3 prices have no statistically significant relationship to competitive entry.¹⁴⁰ Professor Mayo concluded that this “lack of robustness of the econometric results to even simple alternative specifications indicates that the Commission cannot confidently rely on [the results of Professor Rysman’s regressions].”¹⁴¹

Second, as noted in the peer reviews,¹⁴² the regressions do not account for the fact that, in many cases, the reported prices were set in negotiated contracts that cover multiple locations, often in multiple states. Because these contract prices are for a mix of locations – some in areas with multiple BDS providers and some with no BDS providers – there is no basis for concluding that the price observed in any one location reflect the competitive conditions in just that location. Rather, the prices in these contracts will reflect market conditions across all of the locations governed by the contract. For these reasons as well, the regression analyses, which assume that the price in any given location responds only to the competitive conditions in that location, are flawed.¹⁴³

Third, in other respects as well, the pricing data are incorrect or incomplete.¹⁴⁴ Drs. Israel, Rubinfeld, and Woroch, for example, demonstrated the data used in the regressions include DS1 prices that are as high as \$116,353, which is clearly wrong (DS1 circuits generally

¹⁴⁰ *Id.* ¶ 75.

¹⁴¹ *Id.* ¶ 76.

¹⁴² *See, e.g.*, Sweeting First Review ¶ 9.

¹⁴³ *See* IRW Third White Paper at 13.

¹⁴⁴ *See* Sweeting First Review ¶ 9.

cost a few hundred dollars).¹⁴⁵ In addition, the regressions excluded pricing data from circuits that do not have the same bandwidth for all components (*e.g.*, channel termination and local transport) and thus systematically exclude lower priced circuits that rely on multiplexing (*e.g.*, DS3 transport facilities multiplexed to DS1 channel terminations), causing substantial bias in the data.¹⁴⁶ The data also exclude about 42 percent of buildings, and those exclusions are not random.¹⁴⁷ Thus the regressions are based on a highly distorted set of underlying pricing and other data and can dramatically overstate indications of ILEC market power.

Incorrect Measure Of Statistical Significance. As noted, the peer reviews and other economic testimony found that Professor Rysman used an incorrect measure of “standard error” to estimate the statistical significance of his regression results.¹⁴⁸ Professor Rysman himself raised this same concern when he presented his initial results.¹⁴⁹

The problem is straightforward. Where there are two or more circuits in a given area, the standard error used by Professor Rysman treats them as two independent “draws” from a random

¹⁴⁵ See IRW Third White Paper at 13-14.

¹⁴⁶ See *id.*

¹⁴⁷ See *id.*

¹⁴⁸ See, *e.g.*, Sweeting First Review ¶ 23 (“[a] concern with the regressions in Dr. Rysman’s report is that the standard errors have not been clustered” and there is “concern[] that there are some common factors, which mean that customers who are very similar or close geographically will get more similar prices than other customers. Clustering could potentially account for this in a way that is not achieved by the inclusion of fixed, and the common effect of performing clustering is that that standard errors increase.”); Valletti First Review at 7 (“[t]he author acknowledges that it would be interesting to explore the use of cluster standard errors. . . . The correct standard error estimation procedure should be given by the underlying structure of the data”); IRW Second White Paper at 19-20 (“[T]he regressions presented in the Rysman White Paper rely on ‘standard error’ measurement that does not allow for the fact that, in the BDS marketplace, unmeasured factors that determine ILEC pricing are likely to be correlated within each larger area.”).

¹⁴⁹ Rysman White Paper at 26 (“There are basic statistical issues which would be interesting to explore such as the use of clustered standard errors.”).

sample. In fact, they are highly correlated draws because the pricing and competitive conditions among nearby circuits are highly correlated. Accordingly, basic econometrics teaches that a “clustered” standard error should be used.¹⁵⁰ A clustered standard error computes the standard error by grouping correlated observations, rather than treating them as independent draws. The Commission Staff appear to agree: as explained above, the Commission Staff used the clustered standard error approach in its regressions released on June 28, 2016, and this approach had a very substantial effect, making many results no longer statistically significant. However, as discussed above, Drs. Israel, Rubinfeld and Woroch found that the Commission Staff’s approach to computing clustered standard errors is incorrect and, as noted, when done more accurately, even more of the regression results become statistically insignificant.¹⁵¹

Accounting For Different Regulatory Regimes. Professor Rysman’s original regressions examined the relationship between ILEC prices and competitive conditions for all areas together, regardless of the regulatory status in each area, *i.e.*, price cap, Phase I, Phase II. As noted by the peer reviews,¹⁵² this approach masked important differences in these areas. The Commission Staff has re-run the regressions separately for each of these areas. As described above, these new regressions produced nonsensical results, such as findings that ILECs reduce prices in response to competitive entry in areas where ILECs lack the regulatory pricing flexibility to do so. These results thus further vividly confirm that the regression results are often not measuring ILEC market power, but other endogenous factors that overstate the regressions’ measures of ILEC market power.

¹⁵⁰ IRW Third White Paper at 14-15.

¹⁵¹ *Id.* at 24-25.

¹⁵² *See, e.g.*, Sweeting First Review ¶ 25.

Failure To Account For Cable Competition. Professor Rysman’s original regressions failed to account for cable HFC facilities-based competition, and this omission was raised in the peer reviews and by other economists. Indeed, the record shows that cable companies offer high speed data services to business customers using both a version of their residential services and Ethernet services over their widespread HFC facilities.¹⁵³ The cable companies have documented the enormous success they have had in winning business customers with these services, and ILECs and CLECs have documented substantial losses to these cable offerings and their marketplace responses.¹⁵⁴ The Commission Staff tried to address this error by performing additional regressions that account for cable HFC competition. But these new regressions were unable to detect marketplace reactions to this extensive cable competition. As explained by Professors Israel, Rubinfeld, and Woroch, this failure confirms that the regressions are of little

¹⁵³ Comcast 6/28 Comments at 10-17; Cox 6/28 Comments at 10-14; NCTA 6/28 Comments at 25-29.

¹⁵⁴ AT&T 6/28 Comments at 44-46; CenturyLink 6/28 Comments at 38-44; Comments of Verizon, *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. 05-25, RM-10593, at 25-28 (Jan. 27, 2016); Declaration of James A. Anderson, ¶ 33 (Jan. 22, 2016), attached to the Comments of XO Communications, LLC on the Further Notice of Proposed Rulemaking, *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. 05-25, RM-10593 (Jan. 27, 2016); *Ex Parte* Letter from Matthew Brill (Comcast) to Marlene H. Dortch (FCC), *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, at 1-4 (Mar. 25, 2016); *Ex Parte* Letter from Matthew Brill (Time Warner Cable) to Marlene H. Dortch (FCC), *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, at 1-4 (Mar. 25, 2016); Declaration of James Butman on Behalf of TDS Telecommunications Corp., ¶ 5 (Mar. 26, 2015), attached to *Ex Parte* Letter from Thomas Jones (TDS) to Marlene H. Dortch (FCC), *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; Technology Transitions; AT&T Petition to Launch a Proceeding Concerning the TDM-to-IP Transition*, WC Docket No. 05-25, RM-10593, GN Docket Nos. 13-5, 12-353 (Mar. 26, 2015).

use in accurately detecting effects of competition on ILECs.¹⁵⁵ Moreover, Drs. Israel, Rubinfeld, and Woroch further explain that the Commission Staff’s regressions that purport to account for cable HFC competition contain errors (*e.g.*, double counting cable company facilities), and when these errors are corrected, one finds statistically significant pricing effects. Thus, even if (contrary to fact), the Commission’s regressions could be used to assess market power, properly accounting for cable HFC facilities indicates that those facilities do constrain ILEC DS1 and DS3 prices.¹⁵⁶

Staleness of 2013 Data. The peer reviewers and other economists also raised serious questions as to whether any regressions based on 2013 data could provide any useful indication as to the state of competition, including the extent to which ILECs can exercise market power, *today* and going forward.¹⁵⁷ As demonstrated throughout the comments and expert testimony submitted in this proceeding, competition has greatly intensified since 2013, as CLECs, cable companies and others have continued to expand their networks.¹⁵⁸ Indeed, the record shows that since 2013, ILECs have seen reductions in DS1 revenues of **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED] **[END HIGHLY CONFIDENTIAL]** or more, indicating that any market power they may have been able to exercise in 2013 no longer exists today.¹⁵⁹

¹⁵⁵ IRW Third White Paper at 21-23.

¹⁵⁶ *Id.*

¹⁵⁷ *Id.*; Valletti First Review at 6; IRW Second White Paper at 2; Mayo Decl. ¶ 8.

¹⁵⁸ *Notice* ¶ 83 (“The Vertical Systems Group carrier Ethernet leaderboard in recent years also shows rising levels of billable retail Ethernet port installations in the United States, *e.g.*, Ethernet ports grew 26 percent in 2013, 24 percent in 2014, and by more than 20 percent in 2015.”); NCTA 6/28 Comments at 7-8 (noting that CLECs have invested billions into their networks); Comcast 6/28 Comments, at 27-28 (noting that Comcast has invested hundreds of millions of dollars).

¹⁵⁹ AT&T 6/28 Comments at 54.

The Commission has repeatedly brushed aside the staleness (and other deficiencies) of the data on the ground that these are the only data available. But it is clear that the data are incomplete and in some cases unreliable in ways that make them unsuited to the types of regressions the Commission is attempting to perform, and the Commission's insistence that it can still rely on these regression analyses to make a finding of market power and to adopt regulations that will apply indefinitely in the *future* would be the essence of arbitrary decisionmaking.¹⁶⁰

C. The Regression Analyses For Higher Band Services Submitted By Professor Baker, And by Mr. Zarakas And Dr. Verlinda Are Fatally Flawed.

Both Professor Rysman and the Commission Staff have consistently found no evidence of ILEC market power for any BDS services above 50 Mbps in their regressions – results that drive a stake through the heart of the CLECs' proposals for regulation of higher bandwidth services. The CLECs have therefore sponsored two declarations purporting to use regressions to find statistically significant evidence of ILEC market power for such services. These regressions are fundamentally flawed and, in all events, do not support the findings for which they are cited.

1. Professor Baker's Analyses Of Higher Bandwidth Services.

Professor Baker has submitted regressions for higher-band services based on the 2013 data that use the same approach as Professor Rysman to test for the exercise of market power.¹⁶¹ Contrary to Professor Baker's assertions, and as demonstrated by Drs. Israel, Rubinfeld and

¹⁶⁰ See, e.g., *N. Plains Res. Council, Inc. v. Surface Transp. Bd.*, 668 F.3d 1067, 1086 (9th Cir. 2011) (agency action failed when it relied on outdated data and the agency did not show that reliance on several-years-old data could support its conclusions); *Nw. Ecosystem Alliance v. Rey*, 380 F. Supp. 2d 1175 (W.D. Wa. 2005).

¹⁶¹ See Baker Decl., tbl. 1, Regression 1.

Woroch, these tables are based on flawed data and methods and fail to establish that ILECs have market power.¹⁶²

To begin with, Professor Baker’s regressions use the same approach as Professor Rysman’s original regressions, and thus are unreliable for all of the reasons described by the peer reviewers and other economists. Professor Baker’s regressions do not account for endogenous effects, fail to use the proper standard error (clustered standard error) to estimate statistical significance, rely on flawed pricing data, fail to break out different regulatory regimes (price cap, Phase I, and Phase II), and do not account for the substantial increase in competitive activity since 2013. For these reasons alone, Professor Baker’s regressions do not provide any meaningful results.¹⁶³

Even ignoring these flaws and taking Professor Baker’s regressions at face value, they do not establish that ILECs exercise market power. Starting with Table 1, Professor Baker first tests for ILEC market power for high-band (above 50 Mbps) services using census tract fixed effects, and finds no statistically significant results.¹⁶⁴ He then runs the same regression only for what he calls “major providers” (AT&T, CenturyLink, and Verizon), and these tests also show no statistically significant results.¹⁶⁵ He then does a set of regressions that examine the effects separately for the first, second, third, and fourth (or more) in-building and in-census block competitors. Here, he finds nonsensical results:¹⁶⁶ there is no effect on the ILEC when there are one, two, or three competitors in the same census block, but there is an impact on ILECs when

¹⁶² IRW Third White Paper at 26-28.

¹⁶³ *See id.*

¹⁶⁴ *Id.*

¹⁶⁵ *Id.*

¹⁶⁶ *See id.* at 26-27.

there are four or more competitors in the same census block. Similarly, he finds that having one or three rivals connected to the same building has a statistically significant impact on ILEC pricing, but not the if there are two or four or more rivals connected to the same building. In other words, these results are what Professor Rysman described as “muddled and conflicting” and provide no evidence of market power for higher bandwidth services. In all events, Drs. Israel, Rubinfeld, and Woroch show that if Professor Baker had used clustered standard errors, most of his results turn statistically insignificant.

Professor Baker’s only consistent statistically significant results are those in Table 1 and Table 2 that rely upon *county*-level fixed effects techniques. Recall that the “fixed effects” technique is intended to filter out cost, demand and other conditions that cause both lower ILEC prices and greater competitive entry, to ensure that the regression is capturing only the causal relationship between ILEC prices and competitive entry. As Professor Rysman, Commission Staff, and Drs. Israel, Rubinfeld, and Woroch have recognized, the ability of fixed effects techniques to accurately isolate causal effect breaks down for larger geographic areas.¹⁶⁷ That is why Professor Rysman and Commission Staff have based their conclusions on the much smaller census tract level fixed effects analyses (even though they also examined county-level fixed effects). Indeed, it is quite telling that Professor Baker reports only *county* level fixed effects results for Table 2. It is highly likely that he found no consistent statistically significant effects at the census-tract level.¹⁶⁸

¹⁶⁷ See, e.g., IRW Second White Paper at 9-17; IRW Third White Paper at 28; Rysman White Paper at 15.

¹⁶⁸ Given the limited time and the fact that Professor Baker has not produced the computer code and data sets used for his analyses, Professors Israel, Rubinfeld, and Woroch have not been able to independently replicate Professor Baker’s results.

Another serious deficiency in Professor Baker’s regressions is that he did not use clustered standard errors to determine the statistical significance of his results as recommended by the peer reviews (and others), and adopted in Commission Staff’s latest regressions. Drs. Israel, Rubinfeld, and Woroch recomputed the standard errors for Tables 1 and 2 to approximate clustered standard errors, and found that all of the county-level fixed effect regression results turn statistically insignificant.¹⁶⁹

2. Mr. Zarakas’ and Dr. Verlinda’s Analyses Of AT&T’s OC-3 Services Provide No Evidence of Market Power For OC-3 Services.

Sprint also sponsored a declaration submitted by Mr. Zarakas and Dr. Verlinda (the “Zarakas-Verlinda Declaration”), which contains regression analyses purporting to test whether AT&T exercises market power for OC-3 services. These regressions are so fundamentally flawed as to be meaningless. They do not attempt to address the endogeneity issue in any way – indeed, they do not even use fixed effects techniques – which Professor Rysman recognized was a bare minimum necessity. Nor do they use clustered standard errors to estimate statistical significance. And they do not address the multiple other issues identified by the peer reviewers and other economists that undermine the reliability of these types of regressions.¹⁷⁰

¹⁶⁹ See IRW Third White Paper at 28.

¹⁷⁰ *Id.* at 28-30. Mr. Zarakas and Dr. Verlinda also present raw average and median prices for different bandwidth circuits in areas with 0 competitors, one or more competitors, two or more competitors, three or more competitors, and four or more competitors. See Declaration of William P. Zarakas and Jeremy A. Verlinda, tbls. 2.a & 2.b (June 28, 2016) (“Zarakas-Verlinda Decl.”), attached as Exhibit D to the Sprint 6/28 Comments. As explained by Drs. Israel, Rubinfeld, and Woroch, these raw comparisons of average or median circuit prices are meaningless because they fail to isolate any causal relationship between the prices and the number of competitors. IRW Third White Paper at 28-29. It is precisely for this reason that Professor Rysman, Commission Staff, and others use regressions for this type of analyses. In any case, the results of these comparisons do not even facially support claims of market power for OC-3 circuits. For example, these tables show that the average price for an AT&T OC-3 circuit is higher in areas with four or more competitors than in areas with no competitors, which is inconsistent with such claims.

Even overlooking these flaws, the regressions still provide no support for a finding that AT&T has exercised market power for OC-3 services. The Zarakas-Verlinda Declaration presents three regressions, with the third one (“Specification 3”) being the most detailed. This regression examines the relationship between AT&T’s OC-3 prices and competitive conditions in the same census block. According to the results of this regression: (1) there is no statistically significant difference in AT&T’s OC-3 prices for the first in-building competitor; (2) AT&T’s prices go down by 60 percent when there are two or more competitors; (3) AT&T’s prices go up by 42 percent when there are three or more competitors. These results are obviously meaningless.¹⁷¹

In all events, as explained by Drs. Israel, Rubinfeld, and Woroch, “most of the statistically significant results in [the Zarakas-Verlinda Declaration] become statistically insignificant when some of the simplest problems are fixed.”¹⁷² For example, when these regressions are computed using clustered standard errors at the census tract level, almost none of the regression results for AT&T’s OC-3 in Specification 3 is statistically significant.¹⁷³

¹⁷¹ IRW Third White Paper at 28-30.

¹⁷² *Id.* at 29.

¹⁷³ *Id.* Sprint also sponsored a declaration by Professor Kwoka. But Professor Kwoka merely presents the results of Professor Zarakas and Verlinda. In this regard, Professor Kwoka acknowledges that “these data are noisy” and that in some cases “a higher price appears to be associated with a greater number of competitors.” Declaration of John Kwoka Decl. ¶ 28 (“Kwoka Decl.”), attached as Exhibit A to the Sprint 6/28 Comments. He also acknowledges that many of the regressions fail to produce statistically significant results. *Id.* Nonetheless, Professor Kwoka declares all of the regression results that do not support a finding of ILEC market power as “implausible and uninformative” and thus bases his conclusions only on the non-positive and statistically significant results. *Id.* Professor Kwoka also cites to evidence that in other industries, more than one competitor may be needed to achieve reasonably competitive outcomes. But the regressions do not support those conclusions for the BDS marketplace. Indeed, as the Commission, DOJ, and other economists have found, two providers are generally sufficient to ensure competitive outcomes in the BDS marketplace. *See supra* at 39. And, in all

II. THE CLEC PROPOSAL TO ADD AN ADDITIONAL LAYER OF REGULATION FOR WHOLESALE PURCHASES IS UNNECESSARY AND WOULD IMPEDE INVESTMENT AND SLOW THE TRANSITION TO IP-BASED SERVICES.

A handful of CLECs argue that they should be entitled to purchase “wholesale” BDS services at prices substantially below those of “retail” and mobile customers.¹⁷⁴ These CLECs argue that ILECs’ wholesale prices (mainly for Ethernet) are often higher than ILECs’ retail prices, which makes it difficult for CLECs to compete against ILECs for retail customers using ILEC wholesale inputs. The Commission should reject these claims. Indeed, special “wholesale” rules would be unprecedented and unworkable in the context of these negotiated interstate access services, and notably are not even part of the joint “compromise” proposal submitted by Verizon and INCOMPAS. As Verizon explains, the Commission “need not distinguish between wholesale and retail customers” because “[b]oth types of customers receive discounts based on business considerations rooted in economics, rather than based on some arbitrary identity.”¹⁷⁵ Verizon further explains that “a contrary approach could lead to mischief” as “[s]ome carriers might be inclined to try to distinguish between their common carrier offerings as applying solely to retail customers, which could deny their competitors access to the same services.”¹⁷⁶

In this instance, Verizon is correct, but as demonstrated below, there are multiple additional reasons why the Commission should reject these requests. First, the Commission has long held that sections 201 and 202 do not permit discounts reserved for particular classes of events, the regressions do not even support *that* conclusion insofar as the most detailed one found *higher* prices when there were three or more competitors.

¹⁷⁴ Windstream 6/28 Comments at 36-39; Sprint 6/28 Comments at 73-77; TDS 6/28 Comments at 23.

¹⁷⁵ Verizon 6/28 Comments at 9-10.

¹⁷⁶ *Id.* at 10; *see also id.* (claiming that it “has experienced this as a buyer of Business Data Services” from cable companies).

customers, and the CLECs have presented no evidence beyond recycled anecdotes of “price squeezes” that have been repeatedly refuted that would support reversing this decades-old precedent. Nor does the Commission have authority under section 251(c)(4) to mandate wholesale discounts for Ethernet services. The Commission has correctly held that Section 251(c)(4) does not extend to ILEC services like BDS that are predominantly wholesale, and *because* those services are predominantly wholesale ILECs do not have any retail “avoided costs” that could form the grounds for a Section 251(c)(4) discount. And in all events, wholesale discounts under section 251(c)(4) are established through the negotiation and arbitration process supervised by state commissions, not by this Commission.

A. There Is No Legal or Policy Basis For Regulating “Wholesale” BDS Under Sections 201 and 202.

Sprint, TDS, and Windstream argue that the Commission should impose nationwide wholesale discounts under the basic common carrier provisions of Sections 201 and 202.¹⁷⁷ The Commission has no authority to adopt such rules under Sections 201 or 202, and even if it did, these CLEC have not come close to making a factual or policy case for such rules.

First, the CLECs do not – and cannot – offer any legal support for their claim that the Commission could adopt such rules under Sections 201 and 202.¹⁷⁸ As AT&T demonstrated, the Commission has never held that these sections give it authority to mandate wholesale discounts for generally available services.¹⁷⁹ To the contrary, such discounts would be contrary to longstanding Commission precedent interpreting Sections 201 and 202 as prohibiting customer

¹⁷⁷ Windstream 6/28 Comments at 39; Sprint 6/28 Comments at 87-91; TDS 6/28 Comments at 4-10.

¹⁷⁸ 47 U.S.C. §§ 201, 202. *See* Sprint 6/28 Comments at 76-77; *Notice* ¶ 443.

¹⁷⁹ AT&T 6/28 Comments at 66.

or use restrictions – *i.e.*, restrictions that categorically deny certain customers the same rates, terms, and conditions available to others – as unreasonably discriminatory.¹⁸⁰

A rule mandating that carriers give one rate to “wholesale” customers and a different rate to “retail” customers would be a classic unlawful customer or use restriction under these longstanding precedents. The carrier in this situation is providing the exact same service to both classes of customer, and thus there would be no basis in Sections 201 or 202 to permit (much less require) a carrier to charge a higher rate to the retail customer, or to restrict the uses to which the “wholesale” carrier could put the service (*i.e.*, by requiring that carrier to use it only for resale).

That is not to say that there are not other vehicles by which wholesale customers can and do obtain steeply discounted services. For decades, wholesale customers of various services, including BDS, long-distance services, and others, have been able to obtain price discounts through term and volume plans. Under the Act, however, any customer willing to meet the terms of such an offering may purchase it. Indeed, depending on their circumstances, some “retail” customers purchase service with term and/or volume discounts and some “wholesale” customers purchase service at month-to-month rates. But the Act does not authorize carriers to discriminate on the basis of whether customers that are otherwise similarly situated intend to use the services they purchase for retail or wholesale purposes.

¹⁸⁰ *Id.* at 66-67 & n.187. *See, e.g.*, 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, ¶ 111 (1987); 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).

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That Sections 201 and 202 do not authorize the Commission to mandate wholesale discounts for interstate access services is confirmed by sections 251 and 252 of the Act. Those provisions set forth requirements governing the provision of wholesale services, including, which carriers must offer wholesale discounts, when those discounts must be offered, how they are to be quantified, and the process by which that takes place. Under established principles of statutory construction, more general statutory provisions are unavailable as sources of regulatory authority where Congress has adopted a comprehensive and much more specific provision to address the subject matter at issue.¹⁸¹ Because Congress has laid out substantive and procedural provisions for wholesale discounts in sections 251 and 252, the Commission does not have authority under section 201 to chart a different course.

Nor, in all events, have CLECs presented any reason why the Commission should abandon decades of precedent by mandating wholesale discounts for Ethernet services under Section 201 (or any other provision of the Act). To the contrary, the record abundantly refutes any notion that it has somehow become unreasonable for ILECs not to offer separate “retail” and “wholesale” rates for Ethernet services and to impose use restrictions on all of their customers to enforce such discrimination. Non-ILECs have deployed facilities virtually everywhere there is demand for BDS and, even as of 2013, had a *greater* overall market share for BDS than ILECs.¹⁸² Non-ILECs are especially successful in the Ethernet space, representing six of the top nine providers in terms of port share.¹⁸³ And none of the regression analyses demonstrates that

¹⁸¹ See, e.g., *Bloate v. United States*, 130 S. Ct. 1345, 1354 (2010) (“There is no question that . . . ‘[g]eneral language of a statutory provision, although broad enough to include it, will not be held to apply to a matter specifically dealt with in another part of the same enactment.’”) (quoting *D. Ginsberg & Sons, Inc. v. Popkin*, 285 U.S. 204, 208 (1932)).

¹⁸² See, e.g., *supra* at 3.

¹⁸³ ETHERNET LEADERBOARD; see also *Notice* ¶ 83, Chart 1.

ILECs have any market power in Ethernet services. There is simply no basis upon which the Commission could conclude that CLECs need wholesale discounts to compete successfully.¹⁸⁴

The only evidence offered in support of the requested wholesale discounts are claims that ILECs are attempting to effect a price squeeze by charging more for wholesale than for retail services. These claims consist mostly of bald allegations that are neither documented nor substantiated. But in all events, even if they were true, they do not demonstrate any need for a wholesale *discount*. At most, they would demonstrate a potential section 202 claim for unreasonable discrimination.

The only CLEC that even tries to provide specific examples in support of its price squeeze claims is Windstream,¹⁸⁵ but it can only repeat allegations from earlier submissions that have been proven to be unfounded. For example, Windstream asserts that “a comparison of the prices for TDM and Ethernet services at the AT&T Kings Point, Florida wire center shows that the tariffed monthly price for a 1.5 Mbps circuit, *i.e.*, a DS1 connection, is \$126 per month under a 36-month commitment plan, while AT&T’s wholesale Guidebook lists the price of a

¹⁸⁴ As AT&T previously explained, the *Notice’s* Figure 9 shows that non-ILEC providers earn more in revenues from *all* BDS services (TDM and Ethernet) than do ILECs. Competitive providers earned \$23 billion of the \$45 billion in BDS revenues for 2013, and those figures do not include cable company revenues. *See Notice* ¶ 217, Figure 9; see also *id.* at 216, tbl. 1 (Rysman White Paper presenting similar figures). To be sure, the non-ILEC competitors in these data include both traditional CLECs and the ILECs’ out-of-region operations, which for these purposes are no different than traditional CLECs. But the fact that these non-incumbent providers together have won more than half the revenues in the BDS marketplace is powerful proof that incumbent LECs cannot exercise market power and that the ILECs’ “wholesale” BDS offerings do not preclude CLECs from achieving broad-based success in the marketplace.

¹⁸⁵ Sprint provides no evidence of its alleged price squeezes. Instead, it points to allegations made by XO, which AT&T has refuted (*see* AT&T 2/19 Comments at 47-49) and that XO has not repeated. Sprint also relies on allegations made by Windstream, which are addressed herein. TDS relies on an undocumented and unverifiable third party study that it supposedly commissioned. TDS 6/28 Comments at 24-25. It is impossible to determine whether the analyses in this study are valid, or even whether it found widespread issues, or just minor isolated examples.

comparable Ethernet connection of 2 Mbps with an “Interactive” Class of Service (“CoS”) at \$678 per month on a three-year term plan.”¹⁸⁶ In fact, AT&T’s three-year price for a 2 Mbps Ethernet connection with an “Interactive” CoS is \$470 per month, not \$678 per month.¹⁸⁷ Moreover, Windstream is focusing on one of the most expensive CoS offerings. AT&T also offers this service with a lower CoS for a Guidebook price of only \$310 per month. Further, as Windstream is well aware, wholesale customers generally negotiate prices well below those listed in the Guidebook. Indeed, Windstream admits in the next sentence that it can purchase a 2 Mbps Ethernet Connection for far less.¹⁸⁸ Even then, Windstream’s comparison is erroneous.

First, **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED]

[REDACTED] **[END HIGHLY CONFIDENTIAL]** In addition, Windstream appears to be comparing an end-to-end Ethernet service to the price of a bare DS1 channel termination. An end-to-end DS1 service would cost more, after additional rate elements, such as multiplexing or transport, are added. Without ensuring that the configurations of the Ethernet and DS1 service provide equivalent service, which Windstream has not done, comparisons of Ethernet and DS1 rates are apples-to-oranges.

Windstream also continues to assert that **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED]

¹⁸⁶ Windstream 6/28 Comments at 45.

¹⁸⁷ See AT&T Business Service Guide, at 25, available at http://serviceguidenew.att.com/sg_flashPlayerPage/ASE.

¹⁸⁸ Windstream 6/28 Comments at 53.

¹⁸⁹ AT&T 2/19 Comments at 50.

[REDACTED]
[REDACTED]
[REDACTED] [END HIGHLY CONFIDENTIAL] But Windstream does not identify where these prices are being offered, what services it is comparing (AT&T offers multiple 50 Mbps Ethernet services), or any other information that would enable AT&T, or the Commission, to validate or refute these assertions. The Commission cannot legitimately rely on these bare assertions to draw any conclusions about the relationship between retail and wholesale rates.

Windstream likewise continues to assert that AT&T [BEGIN HIGHLY CONFIDENTIAL] [REDACTED]

[REDACTED]
[REDACTED] [END HIGHLY CONFIDENTIAL] Again, Windstream does not provide any details that would enable AT&T to determine the voice/50 Mbps Ethernet service to which it is referring. Moreover, Windstream’s reliance on AT&T’s Guidebook prices is highly misleading. For example, Windstream can purchase a 50 Mbps switched Ethernet connection from AT&T for less than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED]

[REDACTED] [END HIGHLY CONFIDENTIAL]

In short, no CLEC has presented any marketplace evidence that would justify a mandatory “wholesale” discount. Yet any such mandate would impose needless administrative costs on the industry and retard investment and expansion of Ethernet facilities. Retail Ethernet

¹⁹⁰ Windstream 6/28 Comments at 41-42.

¹⁹¹ *Id.* at 42.

services are typically sold as part of a larger bundle that includes multiple unregulated services, and keeping track of when the mandated wholesale discount is required would be costly. Similarly, there is no administratively simple way to determine which purchasers are “wholesale” or “retail” for these purposes. Given that “retail” and “wholesale” BDS services are identical, the seller would have no readily available means of verifying the uses to which the customer is putting the service (which would, of course, invite gamesmanship and require costly auditing).

B. The Commission Cannot Order Wholesale Discounts Under Section 251(c)(4).

Contrary to assertions made by Windstream and Sprint,¹⁹² the wholesale requirements in Section 251(c)(4) are not an available alternative to Section 201 for adopting nationwide wholesale discounts for BDS. The Commission has already found that the wholesale discount requirement in Section 251(c)(4) does not apply to interstate access services because even though those services are purchased by retail customers they are predominantly wholesale in nature. As the Commission explained, “Congress clearly intended section 251(c)(4) to apply to services targeted to *end user* subscribers, because only those services would involve an appreciable level of avoided costs that could be used to generate a wholesale rate.”¹⁹³ The Commission therefore concluded that “access services” that “are predominantly taken by [wholesalers]” and “not end users” are not subject to Section 251(c)(4).¹⁹⁴

This holding by the Commission is fully apt here. Those CLECs seeking a wholesale discount focus almost entirely on ILEC Ethernet services. But the Ethernet services used by

¹⁹² See Sprint 6/28 Comments at 74; Windstream 6/28 Comments at 39 & n.122; Notice ¶ 443.

¹⁹³ *Local Competition Order* ¶ 874.

¹⁹⁴ *Id.*

AT&T’s wholesale customers are “Layer 2” services that are sold on a predominantly wholesale basis. Thus, wholesale customers, like Level 3, Windstream, and Sprint, combine these Layer 2 services with their own “Layer 3” features that enable additional capabilities (*e.g.*, VoIP), and then resell those services in competition with the Layer 3 services of AT&T and other carriers. Overall, about [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of AT&T’s Layer 2 non-affiliate Ethernet revenues are from wholesale customers. Accordingly, under long-standing Commission precedent, BDS services such as AT&T’s Layer 2 Ethernet services are not subject to Section 251(c)(4).¹⁹⁵ Because Layer 2 Ethernet services are predominantly wholesale in nature, there are, as the Commission expected, no “avoided costs” that could serve as the basis for a section 251(c)(4) discount.

Nor could the Commission adopt a federal rule that mandates a specific nationwide wholesale discount. The Commission’s authority to issue rules implementing Section 251(c)(4) is rooted in the local competition regime. The Supreme Court explained in *Iowa Utilities Board* that Section 251 creates a dual regulatory regime in which the Commission’s authority is limited to establishing rules that govern the proceedings used by state commissions to adjudicate and enforce state-specific interconnection agreements.¹⁹⁶ The Section 251(c)(4) “avoided cost” standard cannot be plucked out of this statutory context and applied in a federal rule directly governing interstate services as if it were a provision in Section 201. To the contrary, as AT&T

¹⁹⁵ To be sure, some retail customers also purchase these Layer 2 services, but as the Commission has held, “[t]he mere fact that fundamentally non-retail services are offered pursuant to tariffs that do not restrict their availability, and that a small number of end users do purchase some of these services, does not alter the essential nature of the services.” *Local Competition Order* ¶ 874.

¹⁹⁶ 525 U.S. at 385 (“the 1996 Act entrusts state commissions with the job of approving interconnection agreements,” although the Commission issues “rules to guide the state-commission judgments”).

demonstrated,¹⁹⁷ if Section 251(c)(4) applies here, it is the state commissions, not this Commission, that would set the specific wholesale discounts to be applied in any given state, which they would do pursuant to a general standard fashioned by the Commission. Such a scheme would balkanize the BDS marketplace into a patchwork quilt of state-by-state agreements, all with different wholesale discounts. Moreover, the end result would be an anomalous regime in which state commissions would have primary ratemaking authority over *interstate* services. Any such scheme would be hopelessly complex and unsuitable for regulating BDS services, and could only increase costs and undermine incentives to invest in BDS, thus harming consumers and competition.¹⁹⁸

In all events, as the Commission understood when it held that section 251(c)(4) does not apply to predominantly wholesale interstate access services, there are no material avoided costs that could become the basis of a Section 251(c)(4) wholesale discount.¹⁹⁹ In describing the types of costs that are contemplated by Section 251(c)(4), the statute speaks of “marketing, billing collection, and other costs that will be avoided by the local exchange carrier,”²⁰⁰ and the Commission’s rules have traditionally identified costs such as “product management and sales,” “product advertising,” “call completion services,” “number services,” and “customer

¹⁹⁷ AT&T 6/28 Comments at 67-68.

¹⁹⁸ Nor could the Commission achieve its stated goal of applying any regulations adopted in this proceeding, including the application of wholesale discounts, on a “technology neutral” basis if it were to rely on Section 251(c)(4), because that section applies only to ILECs. AT&T 6/28 Comments at 68; Comcast 6/28 Comments at 56-57. By its terms, Section 251(c) sets forth “Additional obligations of incumbent local exchange carriers.” The duty established in Section 251(c)(4) therefore applies only to ILECs.

¹⁹⁹ *Local Competition Order* ¶ 874.

²⁰⁰ 47 U.S.C. § 251(d)(3).

services.”²⁰¹ Because, as explained above, AT&T’s Layer 2 Ethernet services are sold predominantly to wholesale customers, virtually all of the marketing, billing, collection and other costs are aimed at wholesale, and these same materials are used for retail sales. This is easily seen from AT&T’s Internet website where the Layer 2 Ethernet retail materials are just a slightly modified version of those on AT&T’s wholesale website, and the “resource” materials (*e.g.*, pdfs, videos and other materials describing services) are largely the same.²⁰² In fact, a comparison of these websites shows that there is generally *more* marketing material available to wholesale customers than retail customers, including videos designed specifically to educate wholesale customers about AT&T’s services.²⁰³ Moreover, AT&T uses the same back office systems for both wholesale and retail sales for Layer 2 Ethernet services, and AT&T has dedicated account teams for both wholesale customers and large retail customers. AT&T thus avoids no significant costs when selling these services to wholesale customers, and any costs AT&T does avoid are offset by wholesale-specific costs.²⁰⁴

Given that the ILECs do not, in fact, avoid costs when they provide Ethernet services at wholesale, it should come as no surprise that the methods for computing wholesale discounts

²⁰¹ 47 C.F.R. § 51.609(c)(1).

²⁰² *Compare* AT&T, “AT&T Wholesale”, [https://www.business.att.com/wholesale/Portfolio/solutions with AT&T, “Ethernet Services,”](https://www.business.att.com/wholesale/Portfolio/solutions%20with%20AT&T,%20%E2%80%9CEthernet%20Services,%20%E2%80%9C) <https://www.business.att.com/enterprise/Family/network-services/ethernet>.

²⁰³ *See, e.g.*, AT&T, “Entrance Facility Construction for AT&T Switched Ethernet,” *available at* <https://vimeo.com/160623281>.

²⁰⁴ TDS argues that the fact that AT&T pays a commission to agents for AT&T’s Layer 3 services is evidence that AT&T avoids costs. TDS 6/28 Comments at 21. This argument is a red herring. First, the services at issue here are Layer 2 services, not Layer 3 services. Second, AT&T does not avoid costs by using sales agents. Whether AT&T is selling to a retail or wholesale customer, AT&T incurs costs to make the sale. These costs are either incurred directly by AT&T or indirectly through commissions to sales agents. Either way, AT&T incurs the costs and does not avoid them.

proposed by the CLECs (mainly TDS) are arbitrary. TDS argues that “[o]n an annual basis, the Commission should collect from each price cap ILEC and the Top 5 Ethernet Providers nationwide their 10 lowest retail Ethernet signed contracts rates (net of all discounts) for specified bandwidth in non-competitive markets” and use an “average” of those rates “to determine the benchmark that applies throughout the ILEC’s region.”²⁰⁵

But this proposal does not even purport to gauge avoided costs and therefore does not even get out of the starting gate. Beyond that, AT&T typically offers Ethernet services pursuant to negotiated contracts that often include a variety of other terms and conditions. The Ethernet rates offered in these contracts reflect numerous factors associated with the quid pro quo between AT&T and the purchaser. For example, the Ethernet prices in these contracts typically reflect the fact that the customer is purchasing very large volumes of Ethernet and other services from AT&T. These contracts also sometimes recognize that the customer is offering AT&T discounts on services that AT&T purchases from the customer. It would be patently arbitrary to force AT&T to offer the Ethernet prices in these contracts divorced from the delicate balance of quid pro quos in those contracts. Indeed, Section 202 of the Act expressly allows carriers to offer different rates, terms and conditions to differently situated customers.²⁰⁶ Similarly, AT&T’s prices will often be affected by the location where the services are offered. The prices that

²⁰⁵ Letter from Tamar E. Finn (TDS) to Marlene H. Dortch (FCC) re: Notice of *Ex Parte* Communication, *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 Service*, WC Docket No. 16-143, 15-247, 05-25, RM-10593 (July 21, 2016) (Meeting Handout).

²⁰⁶ 47 U.S.C. § 202(a) (prohibiting only unreasonable differences in pricing among customers); *Competitive Telecommunications Ass’n v. FCC*, 998 F.2d 1058, 1061 (D.C. Cir. 1993) (Section 202 permits “difference” that are “reasonable.”).

AT&T charges in Dallas are not necessarily representative of the prices AT&T offers in Atlanta. Sprint's one-price-fits all approach fails to account for these important differences as well. For all of these reasons, a rule requiring AT&T offer its lowest prices to any customer would reduce AT&T's incentives to offer any of its customers the lowest possible price, even if the customer is willing to give AT&T substantial value in return. Such a requirement therefore could only impede innovative contracts for Ethernet and raise average wholesale prices.

Finally, any attempt to implement additional discounts for wholesale services will dramatically increase the complexity of the revised regulatory regime for BDS proposed in the *Notice*, and could actually lead to *higher* retail rates. For example, a mandatory reduction in wholesale rates would likely put many price cap ILECs below price cap levels. To continue earning reasonable revenues as permitted under the price cap regime, price cap ILECs could be forced to increase retail rates to account for the significant decline in wholesale revenues. This problem would only be exacerbated if the Commission were to order substantial reductions to price caps and adopt an increased X-Factor prospectively.

III. THE COMMISSION SHOULD ADOPT THE COMPETITIVE MARKET TEST PROPOSED BY DRS. ISRAEL, RUBINFELD AND WOROCH, NOT THE ONES PROPOSED BY CLECS.

In its opening comments, AT&T proposed a Competitive Market Test that met all of the Commission's criteria. Under AT&T's proposal, 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.²⁰⁷ As AT&T explained, the data collection confirms that this test constitutes an accurate proxy for census tracts in which almost all of the

²⁰⁷ IRW Second White Paper at 27.

buildings and demand are subject to competition from multiple facilities-based competitors.²⁰⁸ And, the proposal appropriately balances the Commission’s desire for a more geographically granular test with the need to keep the test relatively administrable from the standpoint of both Commission and carrier resources.

The CLECs propose various alternative Competitive Market Tests in which one or more of the key elements – *e.g.*, the geographic unit of regulation (*i.e.*, census tract vs. census block), number of competitors in that geographic unit, whether the competitor must have fiber or a connection, and which services (in terms of bandwidth) are subject to the test – differ from AT&T’s proposal. For example, Verizon’s version of its “compromise” proposal with INCOMPAS would apply the Competitive Market Test to BDS between 50 Mbps and 1 Gbps (with all BDS below 50 Mbps deemed “non-competitive”), and it would treat only those census blocks in which four or more competitors have deployed fiber as competitive. Other CLECs offer even more extreme variations. Perhaps the CLECs believe that by offering extreme proposals they will induce the Commission to accept a slightly less extreme version as a purported middle ground. But, whatever their motive, it is clear that all of these proposals, including the Verizon/INCOMPAS “compromise,” are directly contrary to the data and the Rysman and Commission Staff analysis of those data.

²⁰⁸ The competitive market test includes cable HFC facilities that deployed DOCSIS 3.0 as of 2013 because, as noted, cable companies compete for BDS customers using those facilities. However, even if cable companies’ HFC facilities are *excluded* from the competitive market test, the number of census tracts that pass the test changes only slightly (about 1 percent). IRW Third White Paper at 5 & n.19. Moreover, of those census tracts that pass, the 2013 data still show that more than 90% of ILEC buildings with BDS demand and ILEC bandwidth are within 2,000 feet of at least one other provider’s network (excluding cable companies’ HFC networks).

Census Blocks vs. Census Tracts. Most CLECs argue that the Commission can and should apply the test on a *building-by-building* basis, but, in light of the Verizon/INCOMPAS proposal they say they are willing to “compromise” by accepting census blocks.²⁰⁹

This is hardly a concession at all. Two-thirds of all census blocks with BDS demand contain only a single building (and many others are only a city block). Accordingly, a test that focused on how many competitors were physically “in” a census block would often count a building as non-competitive even if *multiple* CLECs had fiber running *right in front* of that building. Such a result cannot be squared with common sense. Strangely, Verizon expressly concedes this point. It notes that the Rysman analysis “demonstrates that competition outside a given census block may discipline competition within that census block,” and even notes Professor Rysman’s finding that ““competitive supply anywhere in the *Census tract* is correlated in both statistically and economically significant ways with lower prices within the Census block.”²¹⁰ Verizon thinks this makes its proposed census-block test “conservative,” but in fact it would make the test unlawfully under-inclusive. The Commission would have no justification for selecting a geographic basis of relief that it knows, based on the Rysman study, systematically excludes competitors that constrain pricing within that geographic area.²¹¹

Census blocks would also be an administrative nightmare for everyone involved. As AT&T explained, any new test that grants regulatory relief on a geographic basis more granular than the current MSAs will require substantial time and resources to implement. Even once such

²⁰⁹ See, e.g., Level 3 6/28 Comments at 42, 52; Sprint 6/28 Comments at 5-8.

²¹⁰ Verizon 6/28 Comments at 11 (emphasis added) (quoting *Notice* ¶ 238, citing Rysman White Paper at IV.C, tbls. 14-16).

²¹¹ *Motor Vehicle Mfrs. Assn. v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29, 43 (1983) (“Normally, 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[.]”).

a scheme is implemented, sellers and customers alike will continually have to account for the existence of services subject to different regulatory regimes from area to area within the same city. Basing the Competitive Market Test on census blocks will greatly increase the costs and confusion of such a scheme. There are over 11 million census blocks, and a census-block-based rule would likely force carriers and customers to contend with conflicting regulatory regimes from block to block on the same street. Indeed, to avoid such an unworkable patchwork quilt of relief, any sane census-block scheme would likely require some overlay rule to ensure that isolated census blocks did not remain subject to regulation within larger areas where contiguous census blocks met the test for relief. Basing the test on census tracts would more efficiently address that concern, while still providing a much greater level of granularity than the existing MSA-based test. Although still difficult to administer, given that there are 70,000 census tracts, a census tract test would greatly reduce confusion for customers, compliance costs for carriers, and administrative burdens for the Commission as compared with a census block test.

Nearby Fiber vs. Connection. Most CLECs agree that the Competitive Market Test should count competitors that have deployed fiber *near* a building. Indeed, Verizon, again citing Professor Rysman's results, notes that such a test would properly account for the fact that competitors routinely bid for and build to locations in which they have won business. Most CLECs, however, propose a test that would require the competitor to have deployed fiber physically within the geographic area at issue (typically a census block), and Sprint and Level 3 continue to make the more extreme argument that the Commission should count only competitors that have a connection within the relevant geographic area.²¹²

²¹² Sprint 6/28 Comments at 8-12; Level 3 6/28 Comments at 48-51.

The CLECs are again ignoring the data. A “key finding[]” in the *Notice* is that “fiber-based competitive supply within at least half a mile generally has a material effect on prices of BDS . . . ,”²¹³ and both Professor Rysman and Professor Baker made similar findings.²¹⁴ Accordingly, the data lead to a test that would include fiber within 2,000 feet of the census tract, because such a test includes all of the competitors that constrain prices at locations within the census tract. Moreover, the CLECs identify no legitimate basis as to why a provider would only compete for customers nearby its facilities if the provider has already deployed a connection to a building in that area. Indeed, there is no economic or logical basis for assuming that a provider that has deployed sunk network facilities in an areas would forgo profitable opportunities to compete for and win customers at every location near the fiber.

Rather than following the data and the Rysman analysis, the CLECs continue to submit declarations alleging that they can economically build connections to buildings that are only a short distance from their fiber networks. It is important to emphasize, again, that these self-serving declarations are *refuted by the data collection*. For example, Level 3 has submitted a declaration from one its executives presenting an abstract financial analysis purporting to show that it is not economically viable for Level 3 to extend its fiber facilities to locations that demand only 10 Mbps bandwidth, and that Level 3 finds it economically feasible to extend laterals short distances from splice points to locations with bandwidth demand over 50 Mbps and less than 200 Mbps. The actual 2013 data Level 3 submitted in response to the data request show otherwise. Although these data do not identify the distances of Level 3’s builds from its fiber network to individual locations, these data do identify the distances from Level 3 *nodes* to the locations

²¹³ *Notice* ¶ 161.

²¹⁴ *Id.* 208-09 (“a quarter to a half-mile”); Baker Decl. ¶ 43.

where Level 3 has deployed fiber facilities, which include splice points.²¹⁵ Many of Level 3's building connections are not within [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL].²¹⁶ Of the ones that are, [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of the locations with bandwidth demand below 10 Mbps are more than 2,350 feet from the nearest node. Further, [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of Level 3's connections to locations with bandwidth demand between 10 Mbps and 50 Mbps are more than 2,500 feet from the nearest node; [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of Level 3's connections to locations with demand between 50 and 100 Mbps are more than 1,900 feet from the nearest node; and [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] of Level 3's connections to locations with demand between 100 Mbps and 200 Mbps are more than 2,300 feet from nearest node. As Drs. Israel, Rubinfeld, and Woroch demonstrate, the same essential results apply to all CLECs.²¹⁷ The data thus refute the argument that CLECs cannot build to locations with lower levels of demand.²¹⁸

²¹⁵ IRW Third White Paper at 34 (“It is our understanding that nodes include splice points, and are locations from which providers can extend laterals from their existing fiber facilities without having to add a new splice point.”).

²¹⁶ *Id.* (noting that the fact that many Level 3 locations were not near a node suggests that Level 3 either under-reported node locations, or does not always use splice points/nodes when extending lateral connections to buildings, or builds out from nodes at distances longer than the 1,000 meters captured by the FCC's building distance to node crosswalk table).

²¹⁷ *Id.* at 10-11.

²¹⁸ Windstream attempts to use this claimed inability to build out to bait the Commission into reversing years of precedent and requiring ILECs to unbundle DS1 and DS3 loops regardless of whether they are provided over packet-switched, fiber facilities. *See, e.g.*, Windstream 6/28 Comments at 8, 63. The issue of unbundled access to ILEC provisioned packet-switched fiber facilities, however, is beyond the scope of this *Notice*, and Windstream's attempt to insert that issue in this rulemaking should be rejected. *See* Letter from Keith Krom (AT&T) to Marlene H.

Number of Competitors. Many CLECs argue that the Competitive Market Test should require the presence of four competitors before an area is deemed to be “competitive,” while others, notably Verizon, argue merely that it should be “more than two.”²¹⁹ As Drs. Israel, Rubinfeld, and Woroch explain, however, that standard economic analysis establishes that the characteristics of the BDS marketplace ensure that two competitors will produce competitive outcomes.²²⁰ Once a second competitor enters the marketplace and deploys its own facilities-based network, the sunk nature of those investments will drive both competitors to compete fiercely for every available opportunity within reach of those networks.²²¹ In other words, “when there are two BDS providers, both rivals have every incentive to maximize the return on their network investments,” and “purchasers of BDS are typically sophisticated buyers that will seek out the best combination of service quality and price from each competitor.”²²² And as explained

Dortch (FCC), *Technology Transitions*, GN Docket No. 13-5; *Petition for Declaratory Ruling to Clarify that Technology Transitions Do Not Alter the Obligations of Incumbent Local Exchange Carriers to Provide DS1 and DS3 Unbundled Loops Pursuant to 47 U.S.C. §251(c)(3)*, WC Docket 15-1 (Aug. 1, 2016).

²¹⁹ See, e.g., Level 3 6/28 Comments at 43; Letter from Kathleen Grillo (Verizon) and Chip Pickering (INCOMPAS) to Marlene H. Dortch (FCC), WC Docket Nos. 16-143, 05-25, and RM-10593, at 3 (dated August 9, 2016).

²²⁰ IRW Third White Paper at 2 (citing Dennis W. Carlton & Mark A. Israel, *Proper Treatment of Buyer Power in Merger Review*, *Review of Industrial Organization* 39:127-136, at 133 (2011)).

²²¹ *Id.* (“This follows because such investments are in large part economically ‘sunk,’ which means that the relevant variable costs exclude those sunk costs, giving all providers in the area low variable costs to serve new business and thus strong economic incentives to serve the market in the short run and over the longer run. These sunk investments thus thrust rivals into vigorous price competition and the likelihood of such price rivalry imposes an effective constraint on the exercise of market power”).

²²² *Id.*; see also *id.* (“we have seen no evidence in the record to suggest that there are frictions in the BDS marketplace of the type that would mean more than two providers are needed to achieve reasonably competitive results”).

in detail in Section I, *supra*, the regression analyses in the record provide no support whatsoever for the proposition that more than two competitors are necessary to ensure competitive outcomes.

Bandwidth Covered. Most CLECs argue that all services below 50 Mbps should be deemed “non-competitive” everywhere, and in their view the Competitive Market Test would be used to determine areas in which *ex ante* rate regulation would apply to higher bandwidth services (typically up to 1 Gbps).²²³ Such an approach would be directly contrary to the Commission’s analysis of the data. There is no evidence that any ILEC has market power for any services *above* 50 Mbps: Professor Rysman specifically ran regressions to test for market power above 50 Mbps and found no evidence that any such market power existed.²²⁴ All of the Commission’s regression results that it considers to be evidence of market power concern legacy TDM services *below* 50 Mbps and even for those services the Commission did not find that all such services were noncompetitive. Indeed, when those regressions are corrected for errors identified in the peer reviews, they do not support a general finding of market power even for DS1s and DS3s. Accordingly, the only Competitive Market Test that would be consistent with the Commission’s analysis would be to treat all services above 50 Mbps as competitive and apply the test to determine the geographic areas in which to apply *ex ante* rate regulation to DS1s and DS3s. Any other result would violate the one of the most basic principles of administrative

²²³ *See, e.g.*, Verizon 6/28 Comments at 8; Sprint 6/28 Comments at 15-20. Some CLECs propose even more extreme tests: for example, Level 3 would treat all services below *100 Mbps* as non-competitive and apply the CMT only to services above 100 Mbps. Level 3 6/28 Comments at 46-49.

²²⁴ As discussed above, the various regressions performed by Professor Baker and Sprint’s consultants do not establish market power for services above 50 Mbps either.

law, which is that the agency must articulate a “rational connection between the facts found and the choice made.”²²⁵

Ethernet over HFC. Many CLECs argue that the Commission should not count cable companies as a competitor for purposes of the Competitive Market Test when they offer Ethernet over HFC.²²⁶ Here again, the record overwhelmingly establishes that Ethernet over HFC competes directly with BDS. Indeed, NCTA has explained that cable companies are “extend[ing] BDS facilities to new buildings on a daily basis, replacing rapidly vanishing TDM services with superior Ethernet technology and leading the way in the IP transition.”²²⁷ Major cable companies are clearly using Ethernet over HFC to win BDS customers. For example, Comcast boasts of its “broadly available” BDS offerings, explaining that its dedicated Internet access service is “easily scalable and can grow alongside a business without requiring the addition of new lines” and “typically costs less per Mbps than DS-1 or DS-3 services.”²²⁸ Charter has told the Commission that, as a result of its fiber investments, “business services has been one of the fastest growing areas” within the company, with year-over-year revenue growth averaging just under 20 percent.²²⁹ Cox states that it has “been a leader in providing Ethernet

²²⁵ *Motor Vehicle Mfrs. Ass’n*, 463 U.S. at 43 (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156 (1962)); see also *id.* (“Normally, 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[.]”).

²²⁶ See, e.g., Sprint 6/28 Comments at 13-14; TDS 6/28 Comments at 15-16.

²²⁷ NCTA 6/28 Comments at i; see also *id.* at 4-5 (cable companies have made Ethernet marketplace “enormously competitive” and contending that cable Ethernet services “are superior” to legacy services).

²²⁸ Comcast 6/28 Comments at 11.

²²⁹ Letter from John L. Flynn (Charter) to Marlene H. Dortch (FCC) re: Charter Communications Response to FCC’s Information and Data Request, *Applications of Charter Communications, Inc., Time Warner Cable, Inc., and Advance/Newhouse Partnership For Consent to Transfer Control of Licenses and Authorizations*, MB Docket No. 15-149, at 18 (Oct. 16, 2015).

service.”²³⁰ Sprint, one of the principal CLECs advancing this position, just announced plans to provision Ethernet over DOCSIS, relying on existing cable plant, as part of its strategy to offer Ethernet access to “95 percent of the country.”²³¹

Indeed, US Telecom reports the results of a survey of small and medium-sized businesses that shows that most such companies have changed BDS providers within the last few years and 36 percent switched to cable business Internet access (*i.e.*, “best efforts” services).²³² If cable “best efforts” Internet access services are winning business from traditional BDS providers at such rates, then cable Ethernet over HFC must surely be included in the Commission’s Competitive Market Test.

IV. A PROPERLY CALCULATED PRODUCTIVITY-BASED X-FACTOR WOULD BE NO HIGHER THAN 1.99 PERCENT, AND NO ONE-TIME ADJUSTMENT IS WARRANTED.

In its opening comments, AT&T demonstrated that if the Commission intends to change the X-Factor applicable to DS1s and DS3s in “non-competitive” areas, the Bureau of Labor Statistics’ (“BLS”) official measurement of total factor productivity applicable to the communications industry would be the only justifiable public data source for estimating a new productivity-based adjustment.²³³ As Drs. Meitzen and Schoech explained, the BLS data would produce a telecommunications X-Factor of 1.95 percent, if the Commission were to rely on data from 2005-2013 and use GDP-PI to represent national input price changes net of national total

²³⁰ Cox 6/28 Comments at 8.

²³¹ 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>.

²³² USTA 6/28 Comments at 7.

²³³ Other commenters, notably Verizon, agree that the Commission should rely on the BLS KLEMS data. Verizon 6/28 Comments at 15-16.

factor productivity growth.²³⁴ Just as the opening comments were being filed, the BLS revised its total factor productivity statistics and updated them to include data for 2014. Incorporating these revised and updated data into their analysis, Drs. Meitzen and Schoech now show that the BLS data would produce a telecommunications X-Factor of no higher than 1.99 percent, again employing GDP-PI as the national measure for input price growth relative to total factor productivity growth.²³⁵ This updated calculation is practically unchanged from the prior estimate, which provides added confidence that the BLS data are generating a stable estimate of the X-Factor.

As AT&T further explained, both the BLS data and the Rysman study independently establish that there is no basis for a one-time adjustment to the price caps for past productivity gains.²³⁶ More importantly, the Commission Staff's *revisions* to the Rysman study in response to the peer reviewers' criticisms now show even more dramatically that no adjustment would be justified. As part of its revisions, the Commission Staff, for the first time, ran Professor

²³⁴ Mark E. Meitzen & Philip E. Schoech, Assessment of the FCC's Proposed Options for the Special Access Price Cap X-Factor, at 7-9 & tbl. 1 (June 28, 2016) ("Christensen Paper"), attached to Letter from Kyle J. Fiet (AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment; 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 Service*, WC Docket Nos. 16-143, 05-25, RM-10593 (June 28, 2016). As previously explained, Dr. Meitzen and Schoech's calculations involve minor corrections to the Commission's BLS-derived calculations, because the Commission used a method of aggregating KLEMS input price 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.

²³⁵ Christensen Associates, "Reply Comments of Mark E. Meitzen & Philip E. Schoech," *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 Cal 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, at 1-2 (filed Aug. 9, 2016) ("Christensen Reply Comments").

²³⁶ AT&T 6/28 Comments at 8.

Rysman's regressions to test the results separately in areas with different levels of pricing flexibility relief (*i.e.*, Phase II, Phase I, and traditional price caps). If the Commission's theory is that ILEC price reductions in response to increased competitive presence constitute evidence of market power, then we would expect to see the same phenomenon in both Phase II and Phase I areas, because ILECs have the same flexibility to lower rates in Phase I areas as it does in Phase II areas. Although the Commission Staff trumpets such reductions in Phase II areas as evidence of market power, there are *no such reductions* in Phase I areas.²³⁷ In Phase I areas, the regressions show no statistically significant differences in ILEC prices where there is competitive entry and where there is not.

There is only one possible explanation: the price caps *are already set at or below competitive levels*. If that were not the case, one would expect to see price reductions in response to competitive entry in Phase I areas. Thus, the Commission's revised Rysman regressions show conclusively that there is no basis for a one-time reduction in the caps to account for putative productivity gains that were not captured in the prior X-Factor.

No CLEC other than Sprint provides any analysis to support their proposal for a new X-factor or one-time price adjustment, but Sprint's analysis in support of both is baseless.²³⁸ Sprint urges the Commission to ignore the federal government's official total factor productivity data – which do not support any significant adjustment – and instead rely on certain stale data for the U.S. developed by a European Union research consortium known as EU KLEMS. Sprint argues

²³⁷ Commission Staff Response, Attachment 2.

²³⁸ *See, e.g.*, Windstream 6/28 Comments at 60-62; Sprint 6/28 Comments at 46. Verizon again offers no specific proposal but warns the Commission to be careful not to suppress TDM rates too much because it will retard the development of Ethernet. *See* Verizon 6/28 Comments at 14-15.

that these EU KLEMS data support a one-time price reduction of 25-47 percent and a going-forward X-Factor of 4.4 percent.²³⁹

Sprint's proposed data are inapt, for several reasons. First, Sprint's main argument is that the EU KLEMS data are better than those provided by the BLS because they include only the telecommunications industry, whereas the BLS' U.S. KLEMS data also include the broadcasting industry, which Sprint claims drags down the productivity estimates. In fact, as clearly indicated in EU KLEMS documentation of the U.S. data, the measure that it captions "Telecommunications" combines the data from both the telecommunications and broadcasting industries. Accordingly, Sprint's discursive contentions concerning broadcasting productivity relative to pure telecommunications productivity are without any empirical support – and in all events, broadcasting is such a small portion of the U.S. combined telecommunications and broadcasting industries such that it can have only a tiny effect on productivity or input price estimates for the combined industry.²⁴⁰ In any event, the BLS KLEMS data for the U.S. are superior because they extend through 2014 (whereas EU KLEMS data stop at 2010), and

²³⁹ These are figures which (without any analysis) all of the other CLECs appear to propose as well. *See, e.g.*, INCOMPAS 6/28 Comments at 11; Level 3 6/28 Comments at 69-70. Verizon, INCOMPAS's erstwhile partner, proposes no specific X-Factor at all; it says simply that the Commission should "use the KLEMS data, which provides a public source for industry-level data on input prices and total factor productivity for the telecommunications industry." Verizon 6/28 Comments at 15-16. And as shown above, the KLEMS data would support an X-Factor no greater than 1.99 percent. Significantly, no party – neither Sprint nor any other CLEC – supports the addition of a Consumer Productivity Dividend. Indeed, Sprint argues against the imposition of any such additive. Sprint 6/28 Comments at 58-59. In this respect, Sprint's position is consistent with that of AT&T and Drs. Meitzen and Schoech, who have explained that such an additive would be appropriate only if there were some reason to believe that the regulatory change being adopted would goad ILECs into increased rates of BDS productivity – which is most decidedly not the case here. Christensen Reply Comments at 6 n.16; Christensen Paper at 4; AT&T 6/28 Comments at 61-62.

²⁴⁰ Christensen Reply Comments at 3-4 & n.10.

because BLS KLEMS data measure the productivity of individual U.S. industries on a gross output basis.

This latter point is especially important. The EU KLEMS data measure only the *value-added* productivity of industries, and not industries' productivity in producing their gross output. As a result, these data are completely inapposite for calibrating an X-factor for the Commission's BDS price cap plan. As Drs. Meitzen and Schoech explain, the Commission's price cap system places a cap on the total price that a carrier may charge for BDS – not just the portion of that price that is attributable to the value-added produced by the BDS supplier. That is why, whenever the Commission has used total factor productivity to calculate an X-Factor, it has used gross output productivity measures, which encompass all of the carrier's costs to provide the services at issue. Because the EU KLEMS project was aimed at making inter-country comparisons of individual industries' contributions to each country's overall productivity growth, it chose (appropriately for this purpose) to develop value-added productivity measures for each industry that exclude the contributions of purchased inputs such as energy, materials and services to avoid double-counting across industries. Just as a matter of mathematics, these EU KLEMS value-added productivity measures will always exceed the comparable gross output productivity measure – and typically by a significant amount to the extent that energy, materials and services represent a substantial portion of the industry's total cost.²⁴¹

While the use of a value-added productivity measure instead of a gross output productivity measure is enough to invalidate Sprint's analysis, Sprint compounded its error when it extracted an index for input price growth from the EU KLEMS database that measured only

²⁴¹ *Id.* at 4-5 and Appendix 2.

the growth of intermediate input prices (*i.e.*, energy, materials and services) and neglected any price growth in the two primary inputs used to produce BDS: capital and labor.

But measurement of telecommunications industry total factor productivity and input price growth are only one half of the equation used to develop an X-factor. The other half relates to economy-wide total factor productivity and input price growth. Here Sprint's analyses, while not wrong, are not optimal. As Drs. Meitzen and Schoech explain, Sprint proposes to measure economy-wide TFP and input price growth by using a measure restricted to just the Private Nonfarm Business sector of the national economy. This is in contrast to using TFP and input price growth implicit in the entire domestic economy as represented in GDP-PI. GDP-PI is the measure that the Commission has used since the inception of price caps. GDP-PI is preferable: "because GDPPI comprehensively amalgamates national productivity and input price growth, [and] there is no need to separately determine economy-wide total input price growth and economy-wide total factor productivity growth in the X factor calibration."²⁴² It should be noted, however, that if the Commission were to decide to use BLS estimates for productivity and input price growth in the Private Non-Farm Business sector as its proxy for economy-wide trends (consistent with Sprint's method), this would produce a lower X-Factor. Over the 2005-14 period, use of these proxies for national TFP and input price growth would reduce the calculated BDS X-factor from a GDP-PI-based level of 1.99 percent down to a lower level of 1.72 percent.²⁴³

²⁴² *Id.* at 6.

²⁴³ *Id.*

V. THE COMMISSION SHOULD NOT ISSUE BLANKET REGULATIONS GOVERNING TERMS AND CONDITIONS IN COMMERCIAL AGREEMENTS AND TARIFFS.

The comments confirm that the Commission should reject the proposals in the *Notice* to adopt *rules* that would prohibit certain terms and conditions for all tariffs and commercial agreements.²⁴⁴ Even Verizon, which broadly supports new special access regulation, agrees that the Commission should not further regulate terms and conditions.²⁴⁵ Indeed, the terms and conditions addressed in the *Notice* are fundamentally reasonable.²⁴⁶ And any concerns about particular provisions in particular agreements can and should be addressed on a case-by-case basis through the tariff investigation and complaint processes.

The main CLEC proposal is to extend the findings in the *Tariff Investigation Order* to all tariff plans, contracts, or other agreements.²⁴⁷ This proposal must be rejected out of hand, because there is no evidence in the record to support such blanket prohibitions. In the *Tariff Investigation Order*, the Commission found that the “all or nothing” provisions in those specific tariff pricing plans were unjust and unreasonable “in the context of how [the all-or-nothing

²⁴⁴ AT&T 6/28 Comments at 62-64; Mid-Size ILECs 6/28 Comments at 83-97; Hawaiian Telecom 6/28 Comments at 16-19.

²⁴⁵ Verizon 6/28 Comments at 24-25.

²⁴⁶ See, e.g., Reply 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, at 45-46 (Feb. 26, 2016) (“AT&T Tariff Investigation Reply Br.”).

²⁴⁷ See, e.g., Sprint 6/28 Comments at 86 (urging the Commission to “prohibit the terms and conditions deemed to be unlawful for all BDS services, including Ethernet, and across all geographic markets, whether competitive or non-competitive.”); Joint CLEC 6/28 Comments at 87 (“the Commission to “find that all-or-nothing provisions in incumbent LEC arrangements for the sale of Business Data Services in non-competitive markets are unjust and unreasonable regardless of whether those provisions appear in standard tariffs, contract tariffs, or non-tariffed commercial agreements, and regardless of whether those agreements govern the purchase of [circuit-based dedicated services] or [packet-based dedicated services].”).

provisions] combine to operate with other plan provisions.”²⁴⁸ The Commission made no finding that such provisions are, or even that they could be, categorically unjust and unreasonable in all circumstances. Likewise, the Commission’s findings that certain shortfall and early termination liability provisions in these tariff plans are unjust and unreasonable was based on the specific operations of those tariffs including, for example, findings about ILEC costs of performing the services under those specific tariffs and findings that the modifications required by the Commission would still permit ILECs to obtain the “benefit of the bargain” under those plans.²⁴⁹ There is no evidence in this proceeding that these findings extend to any other tariff plan or commercial agreement.²⁵⁰

The proposals to extend the findings and prohibitions of the *Tariff Investigation Order* (which only addressed agreements that covered TDM-based services) to Ethernet services is particularly unjustified, given the extensive evidence in the record that Ethernet providers do not have market power. Since Ethernet providers who offer unreasonable terms and conditions will lose customers, the Commission has no reason to adopt prescriptive rules, and instead can address any issues as they arise on a case-by-case basis.

Moreover, without evidence that the provisions found unlawful in the *Tariff Investigation Order* are unreasonable in most circumstances, the Commission could only cause more harm than good by adopting blanket prohibitions. Such prohibitions would reduce industry flexibility to implement pro-competitive arrangements. For example, AT&T showed that customers

²⁴⁸ Notice ¶ 102.

²⁴⁹ *Id.* ¶¶ 129-139; 152-154.

²⁵⁰ The CLEC breezily assert that “[t]here is every reason to believe that all-or-nothing provisions” have the “same harmful effects” in all agreements, no matter how they are written or what they govern, but this is baseless speculation – not evidence. See Joint CLEC 6/28 Comments at 86.

experiencing substantial growth in TDM-based services may obtain benefits from the provisions, such as lower costs and greater flexibility.²⁵¹ And the provisions may be pro-competitive and beneficial to customers in numerous other circumstances that the Commission has yet to encounter. Parties therefore should be free to incorporate the provisions into their agreements, and should not be barred by overinclusive, rigid prohibitions.

Windstream argues that, for portability plans with volume commitments, “the Commission should institute a ‘fresh look’ opportunity for tariff discount plans that provides customers with the ability to reset their commitment quantities after each shortfall penalty assessment.”²⁵² But, at least for AT&T, these plans already include “buy down” provisions that permit customers to reduce their commitments. And the *Tariff Investigation Order* has already adopted remedies, as needed, to ensure that these buy down prices are just and reasonable. There is thus no basis to also allow customers to reset their commitments after shortfalls under these plans, and there is no evidence in the record to support such remedies.

Windstream also asks the Commission to require ILECs to count Ethernet purchases towards their volume commitments for TDM-based services.²⁵³ Again, there is no evidence that such a requirement is appropriate or needed. Further, if Ethernet purchases must be counted toward commitment levels, Ethernet purchases must also count when computing commitments. That is the quid pro quo. Allowing Windstream to get the benefits of the portability bargain without giving the ILEC commitments on which those benefits are based would be an unfair bargain, and any requirement that ILECs offer such bargains would be patently arbitrary. In all events, the record shows that there is no need for Commission intervention to achieve these

²⁵¹ AT&T 6/28 Comments at 84.

²⁵² Windstream 6/28 Comments at 71-72.

²⁵³ *Id.* at 70.

outcomes because the parties are already negotiating terms that address these issues.

Windstream has [BEGIN HIGHLY CONFIDENTIAL] [REDACTED]

[REDACTED] [END HIGHLY CONFIDENTIAL]²⁵⁴

Sprint and the Joint CLECs rehash arguments that they should be allowed to make one time “fresh look” downward adjustment to commitment levels under ILEC portability plans.²⁵⁵ AT&T and other commenters have previously refuted these arguments.²⁵⁶ Indeed, this type of “fresh look” is an extraordinary remedy, and the Commission uses it sparingly because it alters the settled expectations of the contracting parties and their bargained-for benefits. Here, such a remedy is inappropriate because the customers’ obligations and accompanying penalty provisions were essential to the bargains that the sophisticated parties negotiated, and the customers received countervailing benefits in exchange for agreeing to these provisions. The Commission has no reason to abrogate these contracts, and doing so would merely confer an unwarranted windfall on the customers. And contrary to Sprint’s suggestion,²⁵⁷ the circumstances in this case are not analogous to the *Special Access Expanded Interconnection Order*.²⁵⁸ In that proceeding, the Commission ordered a temporary “fresh look” because it had just directed the ILECs to permit special access competitors to collocate in ILEC central offices,

²⁵⁴ See AT&T Tariff Investigation Reply Br. at 33-34.

²⁵⁵ See Joint CLEC 6/28 Comments at 104-106; Sprint 6/28 Comments at 79-82.

²⁵⁶ See, e.g., AT&T Tariff Investigation Reply Br. at 41-42; Mid-Size ILECs 6/28 Comments at 96-97; Verizon 6/28 Comments at 24-25.

²⁵⁷ Sprint 6/28 Comments at 80 & n.308.

²⁵⁸ See, e.g., Report and Order and Notice of Proposed Rulemaking, *Expanded Interconnection with Local Telephone Company Facilities; Amendment to the Part 69 Allocation of General Support Facility Costs*, 7 FCC Rcd. 7369, ¶¶ 201-02 (1992).

thus creating a brand new source of competition. Rather than waiting for existing term and volume discount plans to expire, the Commission gave long-distance carriers a brief opportunity to switch to the new competitors without have to pay the full termination penalties. There is no such epoch-defining event here; special access competition has existed for years and the record confirms that the CLECs routinely take advantage of the plans to move circuits.

There is likewise no legitimate basis for granting Level 3's new proposal to require ILECs to allow customers to retain discounts they obtained under term plans (*e.g.*, 3 or 5 year plans) on a month-to-month basis in perpetuity after those plans expire.²⁵⁹ This proposal seeks a Commission prescription of ILEC month-to-month rates, *i.e.*, Level 3 asks the Commission to prescribe month-to-month rates at the same levels as those in whatever term plans it chooses to use. But the establishment of rates requires compliance with the stringent standards for a prescription under Section 205 of the Communications Act, which provides that the Commission may order a carrier to offer its services on different rates or terms only *after* it conducts a hearing and (1) makes definitive findings that the existing charges or practices for these services are “in violation of any provisions of this chapter” and (2) determines “what will be the just and reasonable” charges or practices “to be thereafter observed.”²⁶⁰ There is no evidentiary record in this proceeding that any current ILEC month-to-month rate is unjust or unreasonable, nor is there

²⁵⁹ *Ex Parte* Letter from Thomas Jones (Level 3) to Marlene H. Dortch (FCC), *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 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 (July 27, 2016).

²⁶⁰ 47 U.S.C. § 205; *see also* *AT&T v. FCC*, 487 F.2d 865, 874 (2d Cir. 1973) (holding that 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).

evidence that the rates in whatever term plans a CLEC happens to choose would constitute a just and reasonable month-to-month rate. In short, there is no evidentiary basis on which the Commission could prescribe the month-to-month rates proposed by Level 3.

Finally, the Commission’s proposal to regulate certain alleged “tying arrangements” received no significant support in the comments. AT&T and other commenters showed that IP migration provisions and other provisions that provide customers with credits for upgrading their circuits to Ethernet are pro-competitive and pro-IP transition (not anticompetitive), and are not “tying arrangements” under recognized legal and economic standards.²⁶¹ The pro-competitive nature of these provisions is confirmed by the lack of opposition to them – which is consistent with the fact that some CLECS support these arrangements because they provide them with additional flexibility to manage their transition to IP services.²⁶² The arguments of the proponents of regulating these arrangements are insubstantial. The Joint CLECs argue that the Commission “should prohibit incumbent LECs from tying the availability of discounts in harmful ways,”²⁶³ without addressing the fact that none of the challenged arrangements actually involves tying.²⁶⁴ The Joint CLECs also concede that a firm must have market power in the

²⁶¹ AT&T 6/28 Comments at 72-77; Mid-Size ILECs 6/28 Comments at 84-88.

²⁶² AT&T 6/28 Comments at 76-77; *see also* Mid-Size ILECs 6/28 Comments at 84 (noting that even the Commission “seems ambivalent in its approach to IP migration provisions”).

²⁶³ Joint CLEC 6/28 Comments at 99.

²⁶⁴ *See* AT&T 6/28 Comments at 74-75 (explaining that the challenged provisions do not involve tying because they do not “condition” a customer’s purchases of TDM-based services on the customer’s agreement to purchase Ethernet services from AT&T); *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 purchase a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.”) (internal quotation omitted).

tying product market in order for the alleged tying arrangement to be anticompetitive,²⁶⁵ but fail to acknowledge that the record overwhelmingly demonstrates the absence of market power in the BDS market. Accordingly, the Commission has no basis to prohibit the challenged provisions.

VI. THE COMMISSION’S DECISION TO WITHHOLD THE PEER REVIEW REPORTS AND THE COMMISSION STAFF’S NEW ANALYSES UNTIL THE REPLY COMMENT ROUND VIOLATES THE APA AND OMB RULES.

The procedures the Commission has adopted in this proceeding violate the APA and the OMB requirements implementing the Information Quality Act (“IQA”). The problematic procedural pattern began in September 2015, when the Commission imposed extremely short deadlines for interested parties to analyze and present their findings about the 2013 data collection, before the Commission had even made the data collection available. Only after various motions and meetings did the Commission give the parties a modest (albeit inadequate) extension of time. At the same time, Commission did not hold *itself* to these deadlines and instead worked behind closed doors with its own outside economist, Professor Rysman, to perform separate analyses of the data. The Commission finally released Professor Rysman’s report on May 2, 2016, at the same time it issued the *Notice* proposing new rules relying largely on this report.

The Commission again gave the parties a compressed set of deadlines to analyze Professor Rysman’s extensive new set of analyses. It turns out, however, that at the time the Commission issued the *Notice*, the Commission *already had in hand* multiple peer review reports highly critical of the methods and assumptions at the heart of the Rysman regression analyses. The Commission did not release those peer review reports until the date opening

²⁶⁵ Joint CLEC 6/28 Comments at 98.

comments were due, June 28, 2016²⁶⁶ – and it released them along with a large new set of regression analyses performed by the Commission Staff (rather than Professor Rysman). And, like Lucy, the Commission again pulled away the football: the Commission disclosed on July 8, 2016 that it had made mistakes in the analyses it released on June 28, 2016, and it issued yet more new sets of regressions and analyses.

These are not the actions of a reasonable and objective agency trying to get to the right answer. These are the actions of an agency that has clearly already made up its mind and is driving towards a pre-determined result before a change of Administration, regardless of the evidence. These actions also violate the spirit and letter of the Administrative Procedure Act (“APA”) and Office of Management and Budget (“OMB”) rules.

The APA requires that an agency provide interested parties with a meaningful opportunity to comment on proposed rules.²⁶⁷ In order for the opportunity to comment to be “meaningful,” the agency must “disclose in detail” the “data upon which [the proposed] rule is based” so that there can be “an exchange of views, information, and criticism between interested persons and the agency.”²⁶⁸ The agency also must provide stakeholders with sufficient time to review and analyze the data so that they can prepare their comments.²⁶⁹

²⁶⁶ Again, this time period was far too short and, moreover, the Commission did not actually release the data that Professor Rysman used for his analyses until mid-May, and it updated the 2013 data set to include information about cable companies HFC facilities – highly relevant here – in early June.

²⁶⁷ See 5 U.S.C. § 553(c); *Rural Cellular Ass’n v. FCC*, 588 F.3d 1095, 1101 (D.C. Cir. 2009) (“[t]he opportunity for comment must be a meaningful opportunity”); *Portland Cement Ass’n v. Ruckelshaus*, 486 F.2d 375, 393 n.67 (D.C. Cir. 1973) (“Obviously a prerequisite to the ability to make meaningful comment is to know the basis upon which the rule is proposed.”).

²⁶⁸ *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 35 (D.C. Cir. 1977); see also *Air Trans. Ass’n of Am. v. FAA*, 169 F.3d 1, 7 (D.C. Cir. 1999) (“the most critical factual material that is used to support the agency’s position on review must have been made public in the proceeding and exposed to refutation”); *Am. Radio Relay League, Inc. v. FCC*, 524 F.3d 227, 243 (D.C. Cir.

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The Commission has not complied with these requirements because it withheld peer reviews of Dr. Rysman’s White Paper that were completed before the *Notice* was issued and only posted them to this docket on June 28, the date of the initial comment deadline.²⁷⁰ That posting contained two peer review reports: one prepared by Andrew Sweeting, University of Maryland College Park, dated April 26, 2016; and one prepared by Tommaso Valletti, Imperial College London and University of Rome, dated April 28, 2016. The *Notice*, which was released on May 2, 2016 (after the Commission had both reports), stated that the Commission “will release peer reviews of [Dr. Rysman’s white paper] when they are completed in the near future”²⁷¹ – a statement that appears to have been untrue. The June 28 posting also included a three-page memo by the Wireline Competition Bureau that described the peer review process and discussed certain of the peer review comments, three Staff papers that addressed issues raised by the peer reviews, and Dr. Rysman’s revised white paper that was modified in light of the peer review reports.

The APA contemplates that interested parties will have an opportunity to file opening comments and reply comments. Here, however, the parties spent the sixty-day period for opening comments analyzing studies that are now superseded by the peer review reports and the

2008) (Tatel, J., concurring) (Commission must disclose redacted portions of the record to petitioners so they could “mount a substantial evidence challenge”).

²⁶⁹ *Prometheus Radio Project v. FCC*, 652 F.3d 431, 450 (3d Cir. 2011) (meaningful opportunity for comment means “enough time with enough information to comment”); *id.* at 453 (vacating rule where parties did not have adequate time to comment).

²⁷⁰ See Letter from William Layton (Wireline Competition Bureau) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; 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 Nos. 16-143, 15-247, 05-25, RM-10593 (June 28, 2016) (“Layton 6/28 Letter”).

²⁷¹ *Notice* ¶ 164.

additional analyses by Dr. Rysman and Commission Staff. By withholding the peer review reports from interested parties until the comments were filed, and suddenly publishing a new set of studies that supersede the original ones, the Commission has effectively converted the period for reply comments into one for opening comments (and deprived the parties of a reply round). All the parties are basically back at square one. The opening comments were all directed at the Commission's original studies, and thus there is little in the opening comments that is still relevant for reply. The Commission's gambit is particularly troubling because this rulemaking is proceeding on such a compressed time line; the Commission has suggested that it intends to issue an order in September. This leaves commenters with very little time to review the new analyses and respond to other parties' "reply" comments and prepare the sort of carefully considered submissions that the APA contemplates and that are a necessary predicate to Commission action.²⁷² The commenters will have little, if any, time to assess other parties' analyses of the new data and regressions and to submit corresponding *ex partes* before the Commission determines its course of action and prepares and finalizes an order.

The APA violation posed by the Commission's tardy disclosure of the peer review materials and new Staff analyses also implicates the fundamental fairness principles that underlie the APA requirements.²⁷³ The Commission is seeking comment on rule changes that could fundamentally alter the ILECs' rates, services, and contractual arrangements, as well as the workings of the BDS marketplace. It therefore was grossly unfair for the Commission to

²⁷² See *Prometheus*, 652 F.3d at 449 (quoting *Int'l Union, United Mine Workers of Am. v. Mine Safety & Health Admin.*, 407 F.3d 1250, 1259 (D.C. Cir. 2005)) (holding that the APA requires agency "to ensure that agency regulations are tested via exposure to diverse public comment" . . . 'to give affected parties an opportunity to develop evidence in the record to support their objections to the rule and thereby enhance the quality of judicial review'").

²⁷³ *Home Box Office*, 567 F.2d at 35 (the APA's requirements are designed to "provide fair treatment for persons affected by a rule"); *Prometheus*, 652 F.3d at 449 (same).

withhold highly pertinent data until the reply round, and thereby deprive AT&T of sufficient time to provide the agency with their analyses of the data and their considered comments on the proposed Commission actions.²⁷⁴ The core purpose of the APA is to prevent such unjust proceedings.

The Commission's actions also violate OMB rules that govern peer review. The Commission initiated the external peer review of Dr. Rysman's white paper in order to comply with OMB peer review guidelines.²⁷⁵ Those guidelines specify that "important scientific information shall be peer reviewed by qualified specialists *before* it is disseminated by the Federal government," in order to "enhance the quality and credibility of the government's scientific information."²⁷⁶ OMB emphasized that agencies must conduct peer review in a timely manner in order for it to serve its purpose: "it is important to obtain peer review *before* the agency announces its regulatory options so that any technical corrections can be made before the agency becomes invested in a specific approach or the positions of interest groups have hardened," and "[i]f review occurs too late, it is unlikely to contribute to the course of a rulemaking."²⁷⁷ OMB also emphasized that "peer review should precede an opportunity for

²⁷⁴ See *Connecticut Light & Power Co. v. Nuclear Regulatory Comm'n*, 673 F.2d 525, 530-31 (D.C. Cir. 1982) ("An agency commits serious procedural error when it fails to reveal portions of the technical basis for a proposed rule in time to allow for meaningful commentary.").

²⁷⁵ See Layton 6/28 Letter at 1 (citing Final Information Quality Bulletin for Peer Review, Office of Management & Budget, Executive Office of the President, 70 Fed. Reg. 2664 (Jan. 14, 2005)). OMB issued this Bulletin pursuant to its authority under the Information Quality Act, Pub. L. No. 106-554, § 515, 114 Stat. 2763, 2763A-153-154 (2000).

²⁷⁶ *Id.* at 2665 (emphasis added); see also *id.* ("Peer review is one of the important procedures used to ensure that the quality of published information meets the standards of the scientific and technical community").

²⁷⁷ *Id.* at 2668 (emphasis added).

public comment to ensure that the public receives the most scientifically strong product (rather than one that may change substantially as a result of peer reviewer suggestions).”²⁷⁸

At this stage, the Commission has literally placed more than one hundred regressions and revised regressions in the record, all containing mixed and conflicting results. Parties have no way to know which (if any) of these dozens of regressions the Commission intends to rely upon, why it will rely on those regressions and not others, or what conclusions it intends to draw from the regressions it relies upon, or what rules it intends to adopt based on those regressions. The Commission cannot, consistent with the APA’s notice requirements, adopt rules without first providing this information to interested parties and giving them a reasonable opportunity to comment on them. Only with that information can interested parties provide comments directed at the analyses, conclusions, and proposals that are actually on the table. The APA notice requirements are not satisfied merely by releasing a mountain of data and proposing every possible potential rule, leaving interested parties to guess at which of those data points the Commission intends to rely upon and why, and what rules it intends to adopt based on them. The problem is especially acute here, where most of the data was dumped in the record during the *reply* round of comments. Moreover, under the OMB rules, the Commission is supposed to seek peer review of the regressions it ultimately determines to rely upon for its proposed rules and the conclusions it intends to draw from them. For all of these reasons, before the Commission issues new rules in this proceeding, it should provide the information described above to interested parties and give them a proper opportunity to comment, and the Commission should seek peer review of the regressions and conclusions it draws from them upon which any new rules are based.

²⁷⁸ *Id.* at 2670.

CONCLUSION

For the foregoing reasons, the Commission should resolve this proceeding in the manner described above and in AT&T's initial Comments.

Respectfully submitted,

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