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July 21, 2015

ELECTRONICALLY FILED

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: **WC Docket No. 12-375: Rates for Interstate Inmate Calling Services**

Dear Ms. Dortch:

Pursuant to 47 C.F.R. § 1.1206(b)(1), the undersigned submits this written *ex parte* presentation, on behalf of clients with an interest in the provision of Inmate Calling Services (ICS), for filing in the above-referenced docket.

I. Executive Summary

The FCC cannot succeed in its goal of reducing the excessive charges inmates and their families pay for inmate calling services (“ICS”) without addressing site commissions, the single most significant factor causing high calling rates. The FCC recognizes that site commissions are the most significant impediment to reasonable rates for ICS. Any rules that limit or cap ICS rates without also eliminating or reducing the source of high rates are bound to be vacated on judicial review.

For those reasons, the undersigned in a series of *ex parte* filings, has provided the FCC with a roadmap to adopting reasonable limits on the recovery of site commission payments by ICS providers to ensure that ICS remains available to the families of the incarcerated. The undersigned proposes that the FCC establish rate caps for both interstate and intrastate ICS calls that permit providers both (a) to recover their costs, including a reasonable rate of return on investment; and (b) to pay a modest and reasonable, but limited, per-minute site commission to facility owners in those jurisdictions that permit such payments, to provide an incentive for continued availability of ICS in those facilities, while prohibiting carriers from entering into agreements to pay excessive site commissions such as a percentage or share of ICS revenue.

Marlene H. Dortch
July 21, 2015
Page 2

Cap on Recovery of Site Commissions: The FCC should find that a carrier's agreement to pay site commissions in excess of the following maximum per-minute rate levels is an unreasonable practice: Average Daily Population (ADP) of Facility of 1,000 or more - \$0.01; ADP between 300-999 - \$0.02; and ADP below 300 - \$0.03.

Statutory Authority: The FCC has direct legal authority to regulate both intrastate ICS rates and site commissions, under several provisions of the Communications Act.

- Section 201. Under the prohibition on unjust and unreasonable terms, conditions, prices and practices in Section 201(b), the FCC can reject anticompetitive practices that are contrary to the public interest.¹ The FCC has used this power to regulate contractual or other arrangements between common carriers and other entities typically not subject to FCC regulation.²
- Section 276. This section includes requirements that the FCC ensure that all payphone service providers ("PSPs"), including ICS providers, are "fairly" compensated for both interstate and intrastate calls.³ Appellate court precedents confirm that the FCC's authority under this section extends to regulation of rates paid by end-users for intrastate calls.⁴ Excessive site commissions frustrate the FCC's ability to achieve this statutory objective. This section also gives the FCC authority to regulate the negotiations between correctional facilities and ICS providers.⁵
- Ancillary Authority. The FCC's ancillary authority, as set forth in Section 4(i) of the Act provides that the FCC "may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this chapter, as may be necessary in the execution of its functions."⁶ Under this provision, the FCC may regulate when its regulation plainly covers interstate "communication by wire or radio" and its regulations are "rea-

¹ *Applications for Renewal of License Filed by United Telephone Co., of Ohio For Radio Common Carrier Stations KQA459 and KQA651 in the Domestic, Public Land Mobile Radio Service at Lima, Ohio, and Bellefontaine, Ohio*, 26 F.C.C.2d 417, ¶ 6 (citing *NBC v. U.S.*, 319 U.S. 190, 222-223 (1943)).

² *See Promotion of Competitive Networks in Local Telecommunications Markets*, Opinion, 23 FCC Rcd 5385, 5391 ¶ 15 (2008) (citations omitted) (hereinafter referred to as "*Residential MTE Exclusivity Order*").

³ 47 U.S.C. § 276(b)(1)(A).

⁴ *See Illinois Public Telecommunications Ass'n*, 117 F.3d 555, 562 (D.C. Cir. 1997).

⁵ 47 U.S.C. § 276(b)(1)(E).

⁶ 47 U.S.C. § 154(i).

Marlene H. Dortch
July 21, 2015
Page 3

sonably ancillary” to its substantive responsibilities under the Act.⁷ These principles certainly apply to regulating site commissions.

- Regulation of Intrastate Site Commissions. The FCC’s authority under Section 276 extends to each and every call, including both interstate and intrastate calls. The objections from state governments are inconsistent with settled judicial precedent regarding the effect of specific provisions of the Telecommunications Act of 1996 on the general jurisdictional bar set forth in Section 2(b).
- No Authority over Ancillary Charges. The Communications Act, however, generally bars the FCC from regulating non-communications services and this bar prohibits the FCC from regulating ancillary charges

Ratemaking Authority

- The FCC cannot adopt rate regulation that effectively guarantees carriers an economic loss.⁸ Without curbing or limiting site commission payments, but subjecting ICS providers to rate caps, the FCC would effectively guarantee that ICS providers lose money.
- Constitutional principles prohibit the FCC from adopting rate regulations for ICS that are “so unjust as to be confiscatory.”⁹ Under this constitutional principle, the FCC is prohibiting from adopting rate caps that deny ICS providers the ability to recover all of their expenses, including site commission payments.

Correctional Facilities Cost Estimates are Not Reliable

- The FCC has ample grounds to impose reasonable limits on the payment of site commissions. The FCC need not have clear evidence regarding the costs correctional institutions incur but can base its regulation on the use of proxies as it has in other rate decisions. It would be impractical for the FCC to engage in a site-by-site review of such costs.
- The FCC should consider only those costs that are used and useful for the provision of ICS. Correctional facilities have failed to provide sufficient detail regarding their costs that would allow the FCC to meaningfully evaluate the application of this standard to their costs. And those entities that have provided cost studies, such as Cook County, for example, provide enough to detail to demonstrate how correctional facilities inflate their costs and shift the costs of running a correctional facility onto the families of inmates that use ICS.

⁷ *Am. Library Ass’n v. FCC*, 406 F.3d 689, 691-92. (D.C. Cir. 2005).

⁸ *See AT&T v. FCC*, 836 F.2d 1386, 1391-92 (D.C. Cir. 1988).

⁹ *Duquesne Light Co. v. Barasch*, 488 US 299, 307 (1989).

Marlene H. Dortch
July 21, 2015
Page 4

II. Introduction and Background

In previous filings in this docket, filed February 20, 2015; April 8, 2015;¹⁰ May 1, 2015;¹¹ June 1, 2015,¹² and July 1, 2015;¹³ the undersigned has advocated that the FCC, if it is not going to bar site commissions altogether, should permit ICS providers to increase their rates above a strictly “cost-based” level to allow for payment of a reasonable level of site commissions to correctional facilities, despite the fact that the FCC previously held that such commission payments are not recoverable as a cost of service. The purpose of this letter is to summarize the arguments supporting this approach and provide the FCC with a sound legal and factual basis for adopting such a regulatory framework.

Several parties, representing interests as diverse as inmates and their family members (Martha Wright, *et al.*, Petitioners) and ICS providers (Global Tel-Link¹⁴), as well as many sheriffs’ offices, have urged the FCC as a matter of policy to permit some level of payment to correctional facilities. As Petitioners put it in their most recent *ex parte* letter, “while the FCC has the authority to eliminate kickbacks, it should decide to not eliminate kickbacks so that correctional authorities and ICS providers can allocate excess revenue to cover any ICS costs incurred by the correctional facilities[.]”¹⁵ And numerous sheriff’s offices have submitted form letters to the FCC asserting that continued receipt of payments from ICS providers are essential to ensuring the continued offering of this “discretionary” service to inmates.

It is certainly true that, while the FCC has authority to eliminate all site commission payments, it is not required to do so and may decide for policy reasons to adopt a more flexible approach. It is also likely true that correctional facilities do incur *some* costs as a direct result of making ICS available to inmates in their custody, although (as discussed in the undersigned’s February 20 and April 8 letters) the amount of such costs has not been documented in the record with anything near the level of specificity required for the FCC to make cost findings.

¹⁰ Letter from Andrew Lipman to Marlene H. Dortch, (filed April 8, 2015) (“Lipman April 8 *ex parte*”).

¹¹ Letter from Andrew Lipman to Marlene H. Dortch, (filed May 1, 2015) (“Lipman May 1 *ex parte*”).

¹² Letter from Andrew Lipman to Marlene H. Dortch, (filed June 1, 2015) (“Lipman June 1 *ex parte*”).

¹³ Letter from Andrew Lipman to Marlene H. Dortch, (filed July 1, 2015) (“Lipman July 1 *ex parte*”).

¹⁴ Letter from Chérie R. Kiser, Counsel for Global Tel*Link Corporation (“GTL”), to Marlene H. Dortch, (filed April 3, 2015) (“GTL April 3 *ex parte*”).

¹⁵ Letter from Lee G. Petro, Counsel for Petitioners, to Marlene H. Dortch at 1, (filed April 20, 2015) (“Petro April 20 *ex parte*”).

Marlene H. Dortch
July 21, 2015
Page 5

For the reasons outlined in this letter, the FCC should not devote further scarce resources to attempting to develop a more accurate estimate of correctional facility costs. Instead, the FCC should establish a limit on site payments that will provide facilities the ability to cover the reasonable costs of an efficient inmate calling program, and an incentive to continue to offer this valuable service.

Site commission payments should be capped on the basis of cents per minute, and contracts determining payments on the basis of a percentage or share of revenues should be prohibited. Revenue-sharing agreements give correctional facilities and ICS providers a joint interest in increasing the rates paid by consumers, regardless of market forces, and therefore are not in the public interest. A fixed cents-per-minute payment creates no such incentive.

In 2013, the FCC took the historic step of limiting rates for interstate inmate calling services (“ICS”), to protect consumers against excessive rates for a service that, for many, provides the only regular connection to an incarcerated family member or friend.¹⁶ In so doing, the FCC set interim rate caps based on a cost study that expressly excluded any consideration of site commission payments by ICS providers, on the ground that such payments constitute an allocation of profit rather than a cost of service.¹⁷ The rules left ambiguous, at best, the status of site commission payments required under existing and future contracts between ICS providers and correctional facilities.¹⁸ However, the FCC’s rule requiring interstate rates to be based on “cost,” as so defined, was stayed pending appeal by the United States Court of Appeals for the District of Columbia Circuit.¹⁹

The FCC currently is considering proposed rules that would extend rate caps to intrastate ICS, among other things.²⁰ This further rulemaking proceeding gives the FCC an opportunity to revisit

¹⁶ *Rates for Interstate Inmate Calling Services*, 28 FCC Rcd 14107 (2013) (“*2013 Inmate Calling Order*”).

¹⁷ *Id.*, at 14135-38 ¶¶ 54-58.

¹⁸ The record reflects disagreement whether the FCC’s 2013 *Inmate Calling Order* prohibits the payment of site commissions. Compare Letter from D. Baker, Alabama Public Service Commission, Attachment 2 at 2 (filed Jan. 30, 2015) and GTL April 3 *ex parte*, at 8. See also Public Notice, *Wireline Competition Bureau Addresses the Payment of Site Commissions For Interstate Inmate Calling Services*, 29 FCC Rcd 10043, 10044 at 2 (2014). Although the FCC explained that paying site commissions on interstate ICS revenues could be the basis of a finding that a provider’s interstate rates are unjust and unreasonable, some parties argue this does not prohibit payment of site commissions because the FCC also found such payments are a sharing of profit, *2013 Inmate Calling Order*, 28 FCC Rcd at 14135 ¶ 54. In any case, it is clear that the current rules apply only to interstate, not intrastate, rates, so at least commission payments based on intrastate revenue continue to be unrestricted.

¹⁹ *Securus Techs. v. FCC*, No. 13-1280, Order (D.C. Cir. Jan. 13, 2014).

²⁰ *Rates for Interstate Inmate Calling Services*, Second Further Notice of Proposed Rulemaking, 29 FCC Rcd 13170 (2014) (“*Second FNPRM*”).

Marlene H. Dortch
July 21, 2015
Page 6

its treatment of site commissions and ICS rates. However, if the FCC fails to clarify the status of site commissions, or fails to authorize rates that provide a reasonable opportunity for recovery of allowable site commission payments, it risks another stay, or even worse, reversal of its entire ICS regulatory scheme. This paper outlines how the FCC can adopt rules that will avoid that fate.

A. The FCC's Recent Efforts to Reduce Inmate Calling Service Rates

Section 276 of the Communications Act empowers the FCC to regulate both “the provision of inmate telephone service in correctional institutions, and any ancillary services.”²¹ Under § 276(b)(1)(A), the FCC is responsible for ensuring that all payphone service providers—including inmate calling providers—are “fairly[,]” not excessively, “compensated for ... intrastate and interstate call[s] using their payphone[s].”²²

In the *2013 Inmate Calling Order*, the FCC examined in detail the rates charged by providers of ICS and the costs they incurred in order to provide service. The FCC found that ICS rates “in far too many cases greatly exceed the reasonable costs of providing service.”²³ The FCC further discovered that a “significant factor driving ... excessive rates [is] site commission[s]” that ICS providers must pay to correctional facilities in order to obtain the “exclusive right to provide inmate phone service.”²⁴ The FCC determined that site commissions can account for nearly 90 percent of consumer rates,²⁵ and that such payments to correctional facilities are used for numerous non-call-related functions including “inmate welfare to salaries and benefits, states’ general revenue funds, and personnel training.”²⁶

In an effort to reduce ICS rates, the FCC required that ICS rates “be based only on costs that are reasonably and directly related to the provision of [ICS].”²⁷ The FCC then found that site commissions were not costs directly related to the provision of ICS.²⁸ Instead, the FCC determined that site commissions are “an apportionment of profit” between ICS providers and correctional facilities.²⁹ The FCC based this conclusion on the fact that site commission payments are used

²¹ 47 U.S.C. § 276(d).

²² 47 U.S.C. § 276(b)(1)(A).

²³ 28 FCC Rcd at 14110 ¶ 3.

²⁴ *Id.*

²⁵ 28 FCC Rcd at 14125 ¶ 34.

²⁶ *Id.*; *Supra n. 21*.

²⁷ 47 C.F.R. § 64.6010.

²⁸ *2013 Inmate Calling Order*, 28 FCC Rcd at 14135 ¶ 54.

²⁹ *Id.* and at nn.199–200 (citing *2002 Order*, 17 FCC Rcd 3248, 3254–55, 3262–63 ¶¶ 15, 38).

Marlene H. Dortch
July 21, 2015
Page 7

“for a wide range of purposes, most or all of which have no reasonable and direct relation to the provision of [inmate calling].”³⁰

To reach this conclusion, the FCC focused on how correctional facilities use site commission revenues. For example, the FCC found that correctional institutions regularly use the site commissions to fund corrections-related activities and expenses such as “employee salaries and benefits, equipment, building renewal funds, ... and personnel training.”³¹ The FCC further discovered some jurisdictions where a significant percentage, or even all, of the site commissions that correctional facilities collect are treated as general governmental revenue.³² The FCC further found that that some correctional facilities use portions of the commissions they collect to fund inmate welfare programs, *but explained that* such programs have no connection to the provision of ICS.³³

The FCC thus determined that no direct action to reduce site commission payments was needed, instead relying on state government to rein in their growth.³⁴ Some states have limited or eliminated the practice but many have not.³⁵ Thus, the Order failed to take any action that would reduce the largest factor in unreasonably high ICS rates — correctional institution site commissions.

The D.C. Circuit stayed certain aspects of the Order, including the rule requiring that interstate ICS rates “must be based only on costs that are reasonably and directly related to the provision of ICS.”³⁶ Other aspects of the *2013 Inmate Calling Order*, including interim rate caps, remain in effect pending a final decision on review. That review, however, has been abated, pending resolution of the FCC’s subsequent attempt to reduce the unreasonably high charges for ICS.

The *Second FNPRM* demonstrates that the FCC understands the role site commissions play in unreasonably high ICS rates. Even after the FCC adopted interim rate caps on ICS, “failures in the ICS market continue[d].”³⁷ The primary source of market failure is the “pressure to pay site

³⁰ *2013 Inmate Calling Order*, 28 FCC Rcd at 14135-36 ¶ 54-55.

³¹ *Id.* at 14125 ¶ 34 & n.132.

³² *2013 Inmate Calling Order*, 28 FCC Rcd at 14110 ¶ 3 n.13 (“commissions paid to the [Massachusetts] Department of Correction are transferred to the General Fund”); *see also Martha Wright et al. Reply Comments*, Exh. H (filed Apr. 22, 2013) (citing Fla. Stat. § 945.215(b) (2012), Tex. Gov’t Code Ann. § 495.027 (2012), and Wis. Stat. § 3[01].105 (2013) as directing substantial portions of site-commission payments to their respective general treasuries).

³³ *2013 Inmate Calling Order*, 28 FCC Rcd at 14135-36 ¶¶ 54–55.

³⁴ *See id.* at 14137 ¶ 56.

³⁵ *See id.* at 14138 ¶ 58 n. 220.

³⁶ 47 C.F.R. § 64.6010.

³⁷ *Second FNPRM*, 29 FCC Rcd at 13180 ¶ 20.

Marlene H. Dortch
July 21, 2015
Page 8

commissions that exceed the direct and reasonable costs incurred by the correctional facility in connection with the provision of ICS continues to disrupt and even invert the competitive dynamics of the industry.”³⁸

Although the FCC’s rate caps have been effective only for a short period, the FCC recognizes that the interim rate caps “did not completely address the problems in the ICS marketplace.”³⁹ Indeed, the “record is clear that site commissions are the primary reason ICS rates are unjust and unreasonable and ICS compensation is unfair, and that such payments have continued to increase.”⁴⁰

The “payment of site commissions distorts the ICS marketplace by creating ‘reverse competition’ in which the financial interests of the entity making the buying decision (the correctional institution) are aligned with the seller (the ICS provider) and not the consumer (the incarcerated person or a member of his or her family).”⁴¹ This reverse competition exists because “site commission payments are the chief criterion many correctional institutions use to select the ICS provider for their facilities and are thus the main cause of the dysfunction of the ICS marketplace.”⁴²

It is therefore self-evident that reducing or eliminating site commissions would “enable the market to perform properly and encourage selection of ICS providers based on price, technology and services rather than on the highest site commission payment.”⁴³

And it is further obvious that the rate caps adopted in the *2013 Order* have not reduced site commissions. In fact it is the opposite: the FCC found that the level of site commissions *increased* since it developed the record for the *2013 Order*. “Recent contracts show commission payments as high as 96% of gross revenue.”⁴⁴

As the FCC correctly suggested, “[e]liminating the competition-distorting role site commissions play in the marketplace should enable correctional institutions to prioritize lower rates and higher service quality as decisional criteria in their RFPs, thereby giving ICS providers an incentive to offer the lowest end-user rates.”⁴⁵

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.* at 13180-81 ¶ 22.

⁴² *Id.* at 13182 ¶ 24.

⁴³ *Id.* at 13180 ¶ 21.

⁴⁴ *Id.* at 13182 ¶ 26.

⁴⁵ *Id.* at 13183 ¶ 27.

Marlene H. Dortch
July 21, 2015
Page 9

B. Legal Framework

1. The FCC's Authority to Regulate Site Commissions

Multiple provisions of the Communications Act of 1934, as amended (“Act”), provide the FCC with legal authority to limit or prohibit site commissions between inmate calling service (“ICS”) providers and correctional facilities.

a. Section 201

It is well settled that the Act’s prohibition on unjust and unreasonable terms, conditions, prices and practices under Section 201(b) affords the FCC broad power to reject anticompetitive practices that are contrary to the public interest.⁴⁶ The FCC regularly exercised its authority under Section 201(b) to declare carrier practices unreasonable.⁴⁷ An unjust or unreasonable practice can “encompass a broad range of activities provided and rates charged...”⁴⁸ In general, a “practice is deemed anti-competitive to the extent that it harms the competitive process, thereby obstructing “competition’s basic goals -- lower prices, better products, and more efficient methods.”⁴⁹ Because ICS site commissions are a significant factor driving excessive ICS rates,⁵⁰ they should be prohibited as an unreasonable practice.

The FCC’s authority under Section 201(b) to regulate site commissions is not constrained by the FCC’s characterization of site commissions as an apportionment of profits instead of a compensable cost for the provision of ICS.⁵¹ The purpose of that decision was to prevent ICS providers from including site commissions in their interstate rates. Consistent with that goal, the FCC may

⁴⁶ *Applications for Renewal of License Filed by United Telephone Co., of Ohio For Radio Common Carrier Stations KQA459 and KQA651 in the Domestic, Public Land Mobile Radio Service at Lima, Ohio, and Bellefontaine, Ohio*, 26 F.C.C.2d 417, 419 ¶ 6 (citing *NBC v. U.S.*, 319 U.S. 190 at 222-223 (1943)).

⁴⁷ See e.g., *Cable & Wireless*, 166 F.3d 1224 (D.C. Cir. 1999) (failing to follow mandatory international settlement benchmarks); *NOS Communications, Inc. and Affinity Network Incorporated*, Notice of Apparent Liability for Forfeiture, 16 FCC Rcd 8133, 8136 ¶ 6 (2001) (deceptive marketing); *Exclusive Service Contracts for Provision of Video Services in Multiple Dwelling Units and Other Real Estate Developments*, 22 FCC Rcd 20235 (2007) (exclusive clauses in contracts between providers and MDU owners for the provision of video services).

⁴⁸ *Metrophones Telecomm., Inc. v. Global Crossing Telecomm., Inc.*, 423 F.3d 1056, 1068 (9th Cir. 2005).

⁴⁹ *Infonxx, Inc. v. New York Tel. Co.*, Memorandum Opinion and Order, 13 FCC Rcd 3589, 3600 ¶ 21 (1997) (citations omitted).

⁵⁰ *2013 Inmate Calling Order*, 28 FCC Rcd at 14110 ¶ 3.

⁵¹ *Id.* at 14135 ¶ 54.

Marlene H. Dortch
July 21, 2015
Page 10

decide that a site commission is not a compensable cost for setting rates because it has “no reasonable and direct relation to the provision of ICS”⁵² and decide that it is an unreasonable practice that occurs “in connection” with ICS to obstruct lower rates.

Under Section 201(b), the FCC has clear authority to regulate contractual or other arrangements between common carriers and other entities, even those entities that are generally not subject to FCC regulation.⁵³ It may “modify ... provisions of private contracts when necessary to serve the public interest” and has done so when private contracts violate sections 201 through 205 of the Act.⁵⁴ It also has the authority to regulate contracts that “necessarily and inseparably include[]” interstate service as well as intrastate service.⁵⁵ The FCC, for example, prohibited carriers from entering into or enforcing exclusivity clauses in contracts with building owners for the provision of telecommunications services to commercial and residential customers in multiple tenant environments (“MTE”) because such exclusivity arrangements were an unreasonable practice that harmed competition in the telecommunications market.⁵⁶ Such exclusive MTE arrangements included the provision of interstate, international and intrastate telecommunications services. Like those exclusive MTE contracts, correctional facilities generally enter into an exclusive contract that “necessarily and inseparably includes” the provision of interstate and intrastate services, and the FCC therefore has authority to prohibit ICS providers from entering into or renewing contracts that provide for site commissions or regulate the level of such payments.

b. Section 276

Section 276 provides the FCC with broad authority to regulate ICS.⁵⁷ Specifically, Section 276(b)(1)(A) requires the FCC to ensure that all payphone service providers (“PSPs”), including

⁵² *Id.*

⁵³ *Residential MTE Exclusivity Order*, 23 FCC Rcd at 5391 ¶ 15.

⁵⁴ *Id.* at 5392 ¶ 17 (citing *Western Union Tel. Co. v. FCC*, 815 F.2d 1495, 1501 (D.C. Cir. 1987). See also, *Expanded Interconnection with Local Telephone Company Facilities*, CC Docket No. 91-141, Memorandum Opinion and Order, 9 FCC Rcd 5154, 5207-10, ¶¶ 197-208 (1994), *remanded on other grounds*, *Pacific Bell v. FCC*, 81 F.3d 1147 (D.C. Cir. 1996); and *Competition in the Interstate Interexchange Marketplace*, CC Docket No. 90-132, Memorandum Opinion and Order on Reconsideration, 7 FCC Rcd 2677, 2681-82, ¶¶ 23-28 (1992)).

⁵⁵ See *Promotion of Competitive Networks in Local Telecommunications Markets*, First Report and Order and Further Notice of Proposed Rulemaking in WT Docket No. 99-217, Fifth Report and Order and Memorandum Opinion and Order in CC Docket No. 96-98, Fourth Report and Order and Memorandum Opinion and Order in CC Docket No. 88-57, 15 FCC Rcd 22983, 23000 ¶ 35 (2000).

⁵⁶ *Id.* at 23052-53 ¶¶ 160-64 (applicable to commercial customers); *Residential MTE Exclusivity Order* 23 FCC Rcd at 5386, 5391 ¶¶ 5, 14-15 (applicable to residential customers).

⁵⁷ 47 U.S.C. § 276(d).

Marlene H. Dortch
July 21, 2015
Page 11

ICS providers, are “fairly” compensated for both interstate and intrastate calls.⁵⁸ Fairness encompasses both the compensation received by providers and the rates paid by end users.⁵⁹ Site commissions frustrate the FCC’s ability to achieve this statutory objective of “fair” compensation because a correctional facility lacks the incentive to choose the lowest-cost provider and drive ICS rates lower. Existing market forces instead motivate the facility to award its exclusive contract to the ICS provider willing to pay the highest commission, and it is the ICS users and their families and friends that bear the burden of these excessive costs.

The FCC may determine that the existing negotiation process between ICS providers and correctional facilities is anti-competitive. ICS users and their families and friends do not have the option to choose an alternative provider because correctional facilities almost always grant exclusive contracts to a single firm due to security concerns. In contrast, a premise owner in the public payphone market does not have the same need to have a single ICS provider for security measures. Also, unlike correctional facilities, a premise owner wants to increase business at its location and may pay a provider to install a public payphone on the premises to generate value.⁶⁰ Given these differences between the ICS market and the public payphone market, diverse treatment of site commissions under Section 276 is warranted.

The FCC also has authority under section 276(b)(1)(E) to regulate the negotiations between correctional facilities and ICS providers.⁶¹ The statute provides that all PSPs have the right “to negotiate” with the site owner. Clearly, limiting the terms to which regulated carriers can agree in such negotiations falls within the ambit of the FCC’s duty to adopt regulations permitting payphone service providers to negotiate with property owners.⁶² The FCC has adopted a similar position in the context of retransmission consent, where it found that the statute authorizing the agency to regulate “retransmission consent negotiations” permitted the agency to prohibit joint retransmission consent negotiations between one or more of the top four television stations in the same geographic market.⁶³ The FCC took such action because evidence showed that joint negotiations between top four stations increased retransmission consent fees and put pressure on

⁵⁸ 47 U.S.C. § 276(b)(1)(A).

⁵⁹ *2013 Inmate Calling Order*, 28 FCC Rcd at 14115 ¶ 14.

⁶⁰ *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Third Report and Order, and Order on Reconsideration of the Second Report and Order, 14 FCC Rcd 2545, 2616 ¶ 156 (1999).

⁶¹ 47 U.S.C. §276(b)(1)(E).

⁶² One party has argued that this statutory provision actually prohibits the FCC from adopting regulations that limit the potential outcomes of negotiation. This argument was addressed and rebutted in the Reply Comments of Andrew D. Lipman at 3-5 (filed Jan. 26, 2015).

⁶³ *Amendment of the FCC’s Rules Related to Retransmission Consent*, 29 FCC Rcd 3351, 3357 ¶ 19 (2014).

Marlene H. Dortch
July 21, 2015
Page 12

the retail rates charge by distributors.⁶⁴ The site commissions at issue here likewise place upward pressure on the rates ICS providers charge.

The record in this proceeding overwhelmingly demonstrates that the payment of site commissions unreasonably distorts the ICS marketplace and causes unfair compensation. Individual contracts for site commission continue to increase and are as high as 96% of gross revenues.⁶⁵ ICS users and their families and friends spent over \$460 million in 2013 to pay for site commissions⁶⁶ and do not have a seat at the bargaining table regarding the amount or the use of site commissions, which fund a wide range of programs and activities that are not directly related to the provision of ICS. Given the ample evidence in the record, the FCC has the authority to find the paying of site commissions by ICS providers an unreasonable practice and prohibit ICS providers from entering into site commission arrangements with correctional facilities for the provision of ICS. It also has the authority to find site commissions result in payment of unfair compensation by ICS customers.

c. Ancillary Authority

Finally, as a backstop source of authority in addition to the express statutory jurisdiction conferred by the provisions discussed above, Section 4(i) of the Act provides that the FCC may “perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary in the execution of its functions.”⁶⁷ This allows the FCC to take those actions necessary to fulfill the mandate of the Act, even if such actions are not expressly prescribed by the Act. The FCC is therefore not barred from prohibiting site commissions merely because Congress did not explicitly direct the FCC to do so. As the Seventh Circuit explained, “Section 4(i) empowers the FCC to deal with the unforeseen – even if that means straying a little way beyond the apparent boundaries of the Act – to the extent necessary to regulate effectively those matters already within its boundaries.”⁶⁸

Federal courts have long established that the FCC may exercise ancillary jurisdiction when: (1) its general jurisdictional grant under Title I covers the regulated subject and (2) the regulations are reasonably ancillary to the FCC’s effective performance of its statutorily mandated responsibilities.⁶⁹ Courts have come to call the FCC’s section 4(i) power its “ancillary” authority.⁷⁰ The

⁶⁴ *Id.* at 3362 ¶ 16.

⁶⁵ *Second FNPRM*, 29 FCC Rcd at 13182 ¶ 26.

⁶⁶ *Id.* at 13181 ¶ 23.

⁶⁷ 47 U.S.C. § 154(i).

⁶⁸ *North Am. Telecomm. Ass’ v. FCC*, 772 F.2d 1282, 1292 (7th Cir. 1985).

⁶⁹ *Comcast Corp. v. FCC*, 600 F.3d 642 (D.C. Cir. 2010). *See also*, *American Library Ass’n*, 406 F.3d at 691-92.

Marlene H. Dortch
July 21, 2015
Page 13

regulation of ICS providers' contracts for and payment of site commissions easily falls under this framework.

Plainly, ICS is "communication by wire and radio" and thus within the FCC's general grant of authority under Title I of the Act. Correctional facilities argue that payment of site commissions is "too remote from" the provision of ICS to fall within the ambit of the communication by wire and radio jurisdictional grant.⁷¹ There is nothing "remote" about regulating the practices of entities, such as ICS providers, that are "engaged in communication by wire or radio."⁷² Because site commissions are "imposed on ICS providers as a condition of offering ICS, they become part of the cost structure of ICS" and "are among the 'charges, practices, classifications, and regulations for and in connection with' communications services."⁷³ Thus site commissions easily come under the FCC's jurisdiction over the "fair compensation" of ICS providers that offer such service using wire or radio communication.

The cases where courts have found the FCC's regulation did not fall within the Act's general grant simply do not apply. For example, in *Am. Library Ass'n*, the FCC found the FCC lacked authority to regulate television receivers even when such receivers were not providing or receiving communication by either wire or radio.⁷⁴ Similarly, the Seventh Circuit upheld the FCC's refusal to assert authority over the construction of the Sears Tower in Chicago, which purportedly interfered with television transmissions.⁷⁵ Such precedent does not apply here as ICS providers are plainly engaged in communication by wire or radio.

Regulating ICS providers' agreements for and payment of site commission also satisfies the second part of the test for the FCC's ancillary authority because it is "reasonably ancillary" to the FCC's performance of its statutorily mandated responsibilities, namely those set forth in Sections 201(b) and 276(b) that charge the FCC with ensuring that carrier rates remain just and reasonable. FCC "regulation of site commissions is necessary to promote the statutory policy goals of

⁷⁰ *Am. Library Ass'n*, (citing *United States v. Southwestern Cable Co.*, 392 U.S. 157 (1968), *United States v. Midwest Video Corp.*, 406 U.S. 649 (1972) (*Midwest Video I*), and *FCC v. Midwest Video Corp.*, 440 U.S. 689 (1979) (*Midwest Video II*)).

⁷¹ See Georgia Department of Corrections Comments at 11 (filed Jan. 12, 2015). ("Georgia DOC Comments")

⁷² *Accuracy in Media, Inc. v. FCC*, 521 F.2d 288, 293 (D.C. Cir. 1975).

⁷³ Comments of Lattice Incorporated, at 5 (filed Jan. 12, 2015) *citing* 47 U.S.C. § 201(b). ("Lattice Comments")

⁷⁴ 406 F.3d at 703.

⁷⁵ *Ill. Citizens Comm. for Broadcasting v. FCC*, 467 F.2d 1397, 1400 (7th Cir. 1972).

Marlene H. Dortch
July 21, 2015
Page 14

wide availability of ICS and fair compensation “for each and every completed intrastate and interstate call” using correctional facility payphones.”⁷⁶

Further, there is no specific provision of the Communications Act that directly contradicts such an assertion of authority, unlike the assertion of ancillary authority found wanting in *National Ass’n of Regulatory Utility Commissioners v. FCC*,⁷⁷ *Midwest Video II*,⁷⁸ In *NARUC*, the D.C. Circuit rejected the FCC’s claim that its assertion of ancillary jurisdiction over two-way cable data communications was related to its statutory duties pertaining to broadcasting.⁷⁹ In *Midwest Video II*, the Supreme Court rejected the FCC’s assertion of ancillary authority to compel cable companies to make channels available for public access because it conflicted with language in the Act that prohibited the FCC from imposing common carriage regulation on broadcasters.⁸⁰ No such prohibition applies here.

Section 276(b), if it does not directly authorize the FCC to regulate site commission payments, certainly does not prohibit the FCC from adopting such regulations. Prohibiting ICS providers from entering into agreements to pay site commissions, or imposing limits on the permissible range of payments, is plainly a regulation that is “reasonably ancillary” to the FCC’s performance of its statutorily mandated responsibilities under sections 201(b) and 276(b) to ensure that the rates ICS users pay are just and reasonable.

Under these multiple sources of authority, the FCC may prohibit ICS providers from paying site commissions entirely, or alternatively might prohibit them from paying site provisions that exceed a reasonable recovery of legitimate costs incurred by the host facilities caused directly by the provision of ICS on their premises.⁸¹

⁷⁶ Lattice Comments at 6.

⁷⁷ 533 F.2d 601, 612 (D.C. Cir. 1976).

⁷⁸ 440 U.S. at 700-702. In both *NARUC* and *Midwest Video II*, the FCC’s jurisdiction over cable television services was predicated on and thus ancillary to its substantive statutory responsibility over broadcasting since the Act did not, until 1984, directly authorize the FCC to regulate cable television. *See e.g., Southwestern Cable*, 392 U.S. at 178.

⁷⁹ 533 F.2d at 612, 615.

⁸⁰ 440 U.S. at 700-702.

⁸¹ If the FCC elects not to apply such restrictions to *existing* site contracts, at least during their current unexpired terms, then it would have to permit ICS providers to charge rates sufficient to recover those commission payments in addition to their direct costs of offering service.

2. The FCC's Authority Extends to Intrastate Rates

The FCC has express statutory authority, under the plain language of Section 276 of the Communications Act of 1934,⁸² to regulate both interstate and intrastate ICS. Section 276(d) includes ICS in the definition of “payphone service,” and subsection (b)(1) directs the FCC to establish a compensation plan for “all payphone service providers” applying to “each and every completed *intrastate and* interstate call ...”⁸³ Moreover, subsection (c) expressly preempts any State requirements that are inconsistent with the FCC’s regulations.

The FCC correctly outlined the basis for its authority over intrastate rates in the Further Notice of Proposed Rulemaking accompanying the *2013 Inmate Calling Order*.⁸⁴ In addition to citing the statutory provisions noted above, the FCC observed that, in *Illinois Public Telecommunications Ass’n*,⁸⁵ the D.C. Circuit held that the “fairly compensated” provision of section 276(b)(1) empowered the FCC to prescribe rates for local payphone calls. Because the FCC’s authority under that provision includes local rates, it necessarily must include rates for all other intrastate calls.

The FCC also asked for comment on whether Section 2(b) of the Act,⁸⁶ limits its authority to prescribe intrastate ICS rates. The short answer is “no.” The Supreme Court held that amendments to the Act that expressly extend FCC authority to particular intrastate services, like Section 276(b)(1), prevail over the more general terms of Section 2(b) that preserve State authority over intrastate services.⁸⁷

In comments responding to the *2013 Inmate Calling Order*, NARUC argued that the FCC’s interpretation of Section 276 as extending to intrastate ICS rates is contrary to Section 601(c)(1) of the Telecommunications Act of 1996, set out as a note below 47 USC § 152.⁸⁸ The language of that provision directly contradicts NARUC’s position, though. The subsection provides that, the “Act and the amendments made by this Act shall not be construed to modify, impair, or supersede Federal, State, or local law *unless expressly so provided in such Act or amendments.*” (Emphasis supplied.) Section 276(c), which was adopted as part of the Telecommunications Act of 1996, does expressly provide for preemption of State law that is inconsistent with FCC

⁸² 47 U.S.C. § 276.

⁸³ *Id.* at §276(b)(1)(A) (emphasis supplied.)

⁸⁴ 28 FCC Rcd at 14175-78 ¶¶ 135-140, (subsequent history omitted.).

⁸⁵ 117 F.3d at 562.

⁸⁶ 47 USC § 152(b).

⁸⁷ *See AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 380-81 (1999).

⁸⁸ Comments of The National Association of Regulatory Utility Commissioners, at 7 (filed Dec. 20, 2013) (“NARUC Comments”).

Marlene H. Dortch
July 21, 2015
Page 16

regulations relating to payphone services, including ICS. Section 601(c)(1), by its own terms, therefore has no bearing on interpretation of Section 276.

NARUC also attempted to distinguish *Illinois Public Telecommunications* by arguing that the holding in that case only applied to local calls paid for by coins, and could not be extended to intrastate toll calls because “[payphone service providers] have no right to impose long-distance rates.”⁸⁹ This is simply wrong. Payphone service providers (PSPs) can and do set rates for long-distance calls, in the form of sender-paid coin rates for such calls (whether interstate or intrastate).⁹⁰ Thus, as a factual matter, there is no bright-line boundary between local rates charged by PSPs and toll rates charged by IXCs. Indeed, NARUC implicitly acknowledges this elsewhere in its comments, stating that “intrastate toll rates ... are *not always* provided by the payphone equipment owner[,]” implying that they sometimes are.⁹¹

Furthermore, NARUC’s argument ignores crucial language in the court’s holding in *Illinois Public Telecommunications*. In that case, the court was reviewing an FCC order that preemptively deregulated local coin rates, and the States argued that the FCC lacked authority to preempt their regulation of such rates. The court first summarized the petitioners’ argument that

§ 276(b) does not manifest the clear congressional intent necessary to preempt the States’ power over local coin rates. ... Their point is that if the Congress had intended to give the [FCC] jurisdiction over local coin rates, instead of requiring only generally that PSPs be “fairly compensated,” then it would have stated specifically that it was giving the FCC the authority to set the rates for such calls.⁹²

It then squarely rejected this argument, holding that the term “compensation” did include the authority to prescribe regulations governing end user rates, and to preempt inconsistent State regulations:

It is undisputed that *local coin calls are among the intrastate calls* for which payphone operators must be “fairly compensated”; the only question is whether in § 276 the Congress gave the FCC the authority to set local coin call rates in order to achieve that goal.

⁸⁹ *Id.* at 10. *See also, e.g.*, Comments of Securus Technologies, Inc. at 6 (filed Dec. 20, 2013) (arguing that *Illinois Public Telecommunications* court did not consider intrastate toll rates). (“Securus Comments”)

⁹⁰ *See, for example,* <http://www.closetraveler.com/wp-content/uploads/2014/08/public-payphone.jpg> (visited Dec. 8, 2014), and https://en.wikipedia.org/wiki/File:FairPoint_payphone_in_Vermont.jpg (visited Dec. 8, 2014) for photographs of coin telephones offering domestic long-distance calls for 25 cents per minute.

⁹¹ NARUC Comments at 7 (emphasis supplied).

⁹² 117 F.3d at 562.

We conclude that it did. The States' and the NASUCA's argument to the contrary notwithstanding, the Congress has in fact used the term "compensation" elsewhere in the Act in such a way so as to encompass rates paid by callers. ... Because the only compensation that a PSP receives for a local call (aside from the subsidies from CCL charges that LEC payphone providers enjoy) is in the form of coins deposited into the phone by the caller, and there is no indication that the Congress intended to exclude local coin rates from the term "compensation" in § 276, we hold that the statute unambiguously grants the FCC authority to regulate the rates for local coin calls.⁹³

The key element in the court's holding was the conclusion that the statutory term "compensation" encompassed rates paid by callers. The court's discussion referred to rates paid in the form of coins deposited into the phone because that was the only category of rates affected by the FCC regulations under review in that case. Nothing in the court's analysis, however, suggests the method of payment had any bearing on its interpretation of the statutory language. Rather, the italicized language above clearly shows the contrary: that the court considered local coin calls merely as part of a broader class of intrastate calls subject to the FCC's authority under Section 276. Indeed, as noted above, Section 276(b)(1) requires fair compensation for "every intrastate and interstate call[,]" without any distinction between local and toll calls, so there is no basis in the statutory language for the distinction that NARUC seeks to draw.

Similarly, CenturyLink erroneously argued that the FCC "has never ... previously claimed that Section 276 provides it general authority over intrastate end-user rates for any form of payphone services."⁹⁴ In fact, the order reviewed in *Illinois Public Telecommunications* asserted that the FCC had authority to preempt State regulation of end-user rates for local coin calls, and that aspect of the order was affirmed. Just as there is no basis for interpreting Section 276 to limit the FCC's authority to local calls, there is also no basis for an interpretation that would limit that authority to exclude end-user rates.

CenturyLink⁹⁵ also misconstrues the relevant precedent, relying on the D.C. Circuit's decision in *New England Pub Comm'ns. v. FCC*,⁹⁶ for the proposition that the agency's role with respect to intrastate payphone regulation is limited.⁹⁷ But that case did not address the scope of the FCC's authority under Section 276(b)(1)(A); instead, it rejected the argument advanced by PSPs (that

⁹³ *Id.* (emphasis supplied).

⁹⁴ Comments of CenturyLink at 5 (filed Dec. 20, 2013).

⁹⁵ CenturyLink Reply Comments at 7-10.

⁹⁶ 334 F.3d 69, 78 (D.C. Cir. 2003).

⁹⁷ CenturyLink Reply Comments at 9.

Marlene H. Dortch
July 21, 2015
Page 18

was not adopted by the FCC in the order on review) that the FCC should impose the same nondiscrimination and nonstructural safeguards that the agency imposed on the Bell companies to all incumbent local exchange carriers (“ILECs”) generally.⁹⁸ While the D.C. Circuit found that the FCC lacked authority under sections 276(a) (nondiscrimination) and 276(b)(C) (nonstructural safeguards) to impose similar regulations on non-Bell Operating Company ILECs, the case did not call into question the general command in Section 276(b)(1)(a) requiring the agency to adopt a compensation plan providing for fair compensation for intrastate as well as interstate calls.

NARUC also argues that the FCC’s authority under Section 276 is limited to prohibiting discrimination by Bell Operating Companies.⁹⁹ This is both a misreading of the statute and inconsistent with the holding in *Illinois Public Telecommunications*. Although subsection (a) of Section 276 includes provisions specifically prohibiting discrimination by Bell Operating Companies, it is clear that Congress did not intend that subsection to limit the scope of the remaining provisions. Subsection (b)(1) expressly requires the FCC to adopt regulations addressing five specific subjects relating to payphone services, only two of which—clauses (C) and (D)—relate to preventing BOC discrimination. This makes it clear that Congress intended subsections (a) and (b) to address overlapping but not identical subject areas; subsection (a) therefore cannot be interpreted as expressing the sole purpose of the entire section.

Unsurprisingly, a number of State agencies and their representatives, along with a few other parties, dispute the FCC’s authority to adopt regulations affecting the terms and conditions of intrastate ICS, including payment of site commissions. Their arguments largely echo the points addressed above.

For example, some commenters contend that the “purpose” of Section 276 was limited to eliminating Bell Operating Company (“BOC”) discrimination in favor of their own payphones, and that the FCC’s regulations therefore must be restricted to accomplishing that purpose.¹⁰⁰ The statutory language simply does not support this reading; although Section 276(a) deals with BOC payphones, it does not contain any statement of purpose covering the remainder of the section. To the contrary, Section 276(b) *does* contain a statement of purpose: “to promote competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public” The provisions of subsection (b), which includes the FCC’s authority to determine fair compensation, must be construed in harmony with this express statement of Congressional intent, not with an imagined implied intent, apparently derived simply from the fact that the subsection dealing with BOC payphones happened to be placed first.

⁹⁸ See *New England Pub Comm’ns.*, 334 F.3d at 78.

⁹⁹ NARUC Comments at 8.

¹⁰⁰ NARUC Comments at 8; Comments of Inmate Calling Solutions, LLC at 4; Comments of Praeses LLC at 21-22 (filed Jan. 12, 2015) (“Praeses Comments”).

Marlene H. Dortch
July 21, 2015
Page 19

State agencies also argue that because Section 276(b)(1)(A) directs the FCC to ensure that payphone service providers are “fairly compensated for each and every completed intrastate and interstate call using their payphone,” the FCC’s authority under this subsection is somehow limited to ensuring compensation for the use of equipment, and does not encompass rates for telecommunications services.¹⁰¹ This argument flies in the face of the D.C. Circuit’s ruling in *Illinois Public Telecommunications Ass’n*, where the court affirmed the FCC’s authority under Section 276(b)(1)(A) to regulate rates for local telephone calls, which are unquestionably a telecommunications service. No statutory language supports the argument for a supposed equipment/services dichotomy in the FCC’s jurisdiction under this provision.

Several parties try to distinguish *Illinois Public Telecommunications Ass’n* because the case related to local rates, not interexchange services;¹⁰² or because it related to charges paid by coins, not billed to an end user.¹⁰³ There is nothing in the court’s opinion to support such distinctions. The court specifically relied upon the language of Section 276(b)(1)(A), which empowers the FCC to establish fair compensation for “each and every completed intrastate and interstate call[.]” The FCC should reject the verbal gymnastics of those who try to make the statute say something other than what its plain words indicate. “Each and every” means every call of every type, regardless of whether the destination is local or toll, and regardless of whether the charges are paid by coins or by credit card or in some other manner. If, as the court held in *Illinois Public Telecommunications Ass’n*, the FCC has authority to prescribe maximum rates for some payphone calls, the statutory language commands that it have the same authority as to all other calls within the scope of Section 276.

In short, the arguments presented by NARUC and others in an effort to preserve State jurisdiction over ICS rates are contrary to the statutory language and to past judicial construction of the Act, and should be rejected.

3. The FCC’s Regulatory Authority over Ancillary Services is Limited to Communications Services

The *Second FNPRM* proposes to adopt new rules “reforming” ancillary charges imposed by ICS providers, and asks for comments on the scope of the FCC’s legal authority over such charges.¹⁰⁴ Section 276(d) defines “payphone service” as meaning “the provision of public or semi-public pay telephones, the provision of inmate telephone service in correctional institutions, and any ancillary services.” Thus, some class of “ancillary services” is subject to the FCC’s authority under Section 276, but the scope of that class is not defined by the statute.

¹⁰¹ NARUC Comments at 9-10.

¹⁰² NARUC Comments at 11-12; ACC Comments at 6; Georgia DOC Comments at 4.

¹⁰³ *Id.*

¹⁰⁴ 29 FCC Rcd at 13204-5 ¶ 85-86.

Marlene H. Dortch
July 21, 2015
Page 20

A number of parties have urged the FCC to regulate ancillary charges that they characterize as “excessive” or “deceptive,” but very few of these have engaged in any analysis of the FCC’s legal authority to take such action.¹⁰⁵ For example, the Human Rights Defense Center’s argument in support of FCC authority to regulate ancillary charges simply quotes the definitional clause of Section 276(d) noted above, and then asserts without any citation or other support that “[f]ees related to the management of ICS phone accounts fall within the scope of ‘ancillary fees.’”¹⁰⁶ Simply saying this does not make it so.

The FCC, of course, cannot regulate any service unless authorized to do so by Congress because it “literally has no power to act, ... unless and until Congress confers power upon it.”¹⁰⁷ That power must be found in “the language of the statute enacted by Congress. ... [Courts] will not alter the text in order to satisfy the policy preferences” of an administrative agency.¹⁰⁸

The FCC must seek to determine the meaning of the term “ancillary services” in the context in which it was used by Congress in Section 276. The structure of the “payphone services” definition as well as the overall statutory scheme both require that the term “ancillary” be interpreted in a limited sense. The Supreme Court has cautioned that interpretation of a statute must “avoid ascribing to one word a meaning so broad that it is inconsistent with its accompanying words, thus giving ‘unintended breadth to the Acts of Congress.’”¹⁰⁹ A statutory interpretation must be based upon “the language itself, the specific context in which that language is used, and the broader context of the statute as a whole.”¹¹⁰ “A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme ... because only one of the permissible meanings produces a substantive effect that is compatible with the rest of the law.”¹¹¹

¹⁰⁵ See, e.g., Comments of Pay Tel Communications, Inc. at 30-34 (filed Dec. 20, 2013); Comments of Human Rights Defense Center at 9-10 (filed Jan. 12, 2015) (“HRDC Comments”); Reply Comments of Martha Wright *et al.* at 12-16 (filed Jan. 13, 2014); Reply Comments of Pay Tel Communications, Inc. at 18-19 (filed Jan. 13, 2014). Ironically, although Pay Tel devoted extensive attention in both initial and reply comments to the FCC’s legal authority to preempt State regulation of intrastate rates, its arguments in support of limits on ancillary charges were supported by no statutory analysis whatsoever.

¹⁰⁶ HRDC Comments at 9.

¹⁰⁷ *La. Pub. Serv. Comm’n v. FCC*, 476 US 355, 374 (1986).

¹⁰⁸ *Barnhart v. Sigmon Coal Co.*, 534 U.S. 438, 461-62 (2002).

¹⁰⁹ *Gustafson v. Alloyd Co.*, 513 U.S. 561, 575 (1995) (quoting *Jarecki v. G. D. Searle & Co.*, 367 U.S. 303, 307 (1961)).

¹¹⁰ *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341 (1997).

¹¹¹ *United Sav. Ass’n. of Tex. v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 371 (1988).

Marlene H. Dortch
July 21, 2015
Page 21

Here, sections 1 and 2 of the Act provide the general context within which section 276 must be considered. Section 1 declares that the purposes of the Act include “to make available ... a rapid, efficient, Nation-wide and world-wide wire and radio *communication service* with adequate facilities at reasonable charges”¹¹² Section 2(a) specifies that the provisions of the Act apply to “communication by wire or radio”¹¹³ In short, the purpose of the Act is to regulate communications, not to regulate financial transactions or sales of other goods or services. Further, section 276(b)(1)(A) specifies that any compensation plan adopted by the FCC must ensure that providers “are fairly compensated for *each and every completed intrastate and interstate call*”¹¹⁴ “Ancillary services” in section 276(d), therefore, must be construed as meaning *communications* services that are ancillary to the completion of interstate and intrastate ICS *calls*. This could include, for example, charges for operator services or directory assistance that are in addition to the basic per-minute charge for a call.

The FCC’s proposed “reform” of ancillary charges, however, goes far beyond the limits that Congress intended. The *Second FNPRM* proposes to prohibit or cap some types of so-called ancillary charges that are not charges for completion of a call, or even charges for a communications service at all, such as “account establishment by check or bank account debit; account maintenance; payment by cash, check, or money order; monthly electronic account statements; account closure; and refund of remaining balances[.]”¹¹⁵ and money transfer service fees.¹¹⁶ The FCC also asks open-ended questions about possible prohibitions or caps on other, unspecified ancillary charges.

For the reasons explained above, the FCC does not have statutory authority to regulate fees for financial transactions such as electronic fund transfers and other methods of funding an account. These are not charges for communications services, nor are they related to the completion of individual calls. In the *2013 Inmate Calling Order*, the FCC relied on precedent holding that “billing and collection services provided by a common carrier for its own customers are subject to Title II,” and by analogy concluded that it could regulate such services when performed by an ICS provider for its customers.¹¹⁷ That analogy only holds up, however, to the extent that the ICS provider is billing for completed calls, since that is the extent of the FCC’s regulatory duties under Section 276. When the ICS provider is billing a customer for some other service, such as a money transfer, the FCC lacks jurisdiction.

¹¹² 47 USC § 151 (emphasis added).

¹¹³ 47 USC § 152(a)

¹¹⁴ 47 USC § 276(b)(1)(A) (emphasis supplied)

¹¹⁵ 29 FCC Rcd at 13206 ¶ 89.

¹¹⁶ *Id.* at 13213 ¶ 104.

¹¹⁷ 28 FCC Rcd at 14168 ¶ 114.

Marlene H. Dortch
July 21, 2015
Page 22

Numerous parties agree with this analysis.¹¹⁸ On the other hand, parties favoring FCC regulation of ancillary charges generally did not address the question of jurisdiction, but simply assumed that the FCC had the authority and offered policy arguments why it should act. The only notable exception was the Petitioners, Martha Wright *et al.*, who contend that the FCC does have jurisdiction over ancillary charges under Sections 201, 205, and 276.¹¹⁹ Their argument, however, is circular and ignores the jurisdictional structure of the statute. The FCC's authority to prohibit "unjust or unreasonable" charges, classifications, and practices under Section 201(b), and to prescribe just and reasonable charges and practices under Section 205, are both limited to *interstate* communications services under Section 2(b). Although the FCC does have jurisdiction over intrastate ICS under Section 276, as demonstrated in the preceding argument section, its authority to preempt State laws and regulations is limited to that expressly conferred under Section 276. The FCC cannot use Sections 201 or 205 to "bootstrap" itself authority over any intrastate service not within the scope of Section 276. And Petitioners' argument that Section 276 confers this authority is limited to pointing out that the words "ancillary services" appear in the definition of "payphone service" in subsection (d). As discussed above, that language is the starting point, not the conclusion, for an analysis of the FCC's jurisdiction.

In short, none of the commenting parties have offered any persuasive argument for an interpretation of Section 276 that would permit the FCC to regulate financial transactions. The statute simply does not confer that authority, and the FCC therefore cannot prohibit or limit fees for non-communications services.

¹¹⁸ Comments of Global Tel*Link Corporation at 27-30 (filed Jan. 12, 2015); Lattice Comments at 8-9; Comments of Securus Technologies, Inc. at 25 (filed Jan. 12, 2015).

¹¹⁹ Petitioners Martha Wright *et al.* Comments at 16-17.

Marlene H. Dortch
July 21, 2015
Page 23

III. The FCC Must Address Site Commissions

The FCC’s second attempt to rein in unreasonable rates for ICS will fail unless it addresses “site commissions [—] the primary reason ICS rates are unjust and unreasonable.”¹²⁰ As discussed in the following two sections, rules that cap rates on costs that exclude site commissions, but do not prevent correctional facilities from continuing to demand such commissions, would almost certainly be reversed by the Court of Appeals.

First, failing to address site commissions, which the record demonstrates and the FCC declares to be the predominant factor resulting in unreasonably high ICS rates, would be arbitrary and capricious. A regulatory agency cannot “entirely fail[] to consider an important aspect of the problem, offer[] an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.”¹²¹ Site commissions, as those on both sides of the issue readily acknowledge, are an “important aspect” of the ICS problem.¹²²

Second, imposing rate caps on ICS providers that do not permit ICS providers to recover the costs of site commissions while at the same time doing nothing to end the practice of site commissions would necessarily result in rates that are confiscatory in violation of the Fifth Amendment to the Constitution. The FCC cannot set rates at levels so low that they make it impossible for service providers to recover their costs *and* provide a reasonable return on capital to their investors. Excluding site commissions from costs, without any offsetting opportunity for recovery, guarantees this prohibited result.

A. It Would Be Arbitrary and Capricious to Adopt ICS Rate Rules that Fail to Reduce or Eliminate Site Commissions — the Primary Cause of Unreasonably High Rates

In 2013, the FCC decided to ignore an entire category of expenditures by ICS providers — site commissions — by concluding that they are profits, not a cost of service.¹²³ The FCC’s analysis of whether site commissions are direct costs of providing ICS, however, focused exclusively on whether they recover communications-related costs incurred by correctional facilities (correctly concluding that they do not). But it ignored the fact that paying site commissions is an unfortu-

¹²⁰ See *Second FNPRM*, 29 FCC Rcd at 13180 ¶ 21.

¹²¹ *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (internal citations omitted).

¹²² See *Second FNPRM*, 29 FCC Rcd at 13180 ¶ 20. See, e.g., Reply Comments of Lattice, Inc. at 9 (filed Jan. 27, 2015) (noting how “site commissions affect access to ICS”).

¹²³ *2013 Inmate Calling Order*, 28 FCC Rcd at 14135 ¶ 54.

Marlene H. Dortch
July 21, 2015
Page 24

nate cost of doing business for ICS providers,¹²⁴ despite recognizing that these commissions make up an extraordinary high percentage of the expenses ICS providers incur.¹²⁵ It is therefore puzzling that the FCC would consider adopting rate caps based on a cost study that does not consider at all the impact of site commissions on ICS provider expenditures. To ignore such a significant component of ICS provider expenses in setting rates is plainly arbitrary.

The FCC is well aware how curbing site commissions will benefit the ICS marketplace. It found that “[e]liminating the competition-distorting role site commissions play in the marketplace should enable correctional institutions to prioritize lower rates and higher service quality as decisional criteria in their RFPs, thereby giving ICS providers an incentive to offer the lowest end-user rates.”¹²⁶ But the FCC has not yet taken any action that would rein in site commissions. Instead its plan seems to be to wait until state governments decide to prohibit the use of site commissions. Given that many states have used ICS rates to raise funds for their general treasuries,¹²⁷ it seems unlikely that many states will be rushing to enact ICS rate reforms that the FCC itself refuses to adopt.

Further, it is arbitrary for the FCC to establish a compensation regime where regulated carriers are effectively guaranteed an economic loss due to site commission payments¹²⁸. As Securus has explained, “under the Rate Caps, it is economically impossible to continue paying commissions while covering the cost of service and without passing through commissions to end users in the calling rates.”¹²⁹ In *AT&T*, the D.C. Circuit rejected the FCC’s rate of return refund rule, which required carriers to refund any actual returns in excess of the threshold established by the agency.¹³⁰ It did so because the FCC’s refund rule did not allow carriers to offset gains against periods where their actual rate of return was lower than the threshold, and therefore was inconsistent with the rest of the regulatory scheme.¹³¹ The rule seemed to “guarantee the regulated company an economic loss.”¹³² Absent a prohibition on site commission payments, the same principle would apply to ICS providers.

¹²⁴ *Id.* at 14125 ¶ 34 n.132, at 14110 ¶ 3 n.13.

¹²⁵ *Id.*

¹²⁶ *Second FNPRM*, 29 FCC Rcd at 13183 ¶ 27.

¹²⁷ *2013 Inmate Calling Order*, 28 FCC Rcd at 14110 ¶ 3 n.13.

¹²⁸ *See AT&T*, 836 F.2d at 1391-92.

¹²⁹ Letter from S. Joyce, counsel for Securus Technologies, Inc. to Marlene H. Dortch, FCC, at 2 (filed May 4, 2015) (Securus May 4 *ex parte*).

¹³⁰ *AT&T*, 836 F.3d at 1391.

¹³¹ *Id.* at 1390-91.

¹³² *Id.* at 1391.

B. Rate Caps that Ignore Site Commissions Without Restraining the Amount of Site Commissions Will Result in Confiscatory Rates Barred by the Fifth Amendment

The Fifth Amendment to the Constitution protects regulated entities from regulations that are “so unjust as to be confiscatory.”¹³³ *Duquesne* established that to prevail on a claim of a confiscatory regulation, the regulated company must show that the regulation will “jeopardize the financial integrity of the company[y], either by leaving [it] insufficient operating capital or by impeding [its] ability to raise future capital,” or that the regulation results in rates that “are inadequate to compensate current equity holders for the risk associated with their investments under a modified prudent investment scheme.”¹³⁴

Here, the FCC has established rate caps based on ICS provider cost studies that specifically exclude the cost of paying site commissions, even though those commission payments are the primary reason for excessive rates.¹³⁵ Thus the rate caps limit the ability of ICS providers to obtain revenues that exceed their cost. Accordingly, ICS providers will not be able to remain in business if they must comply with the FCC’s rate caps, while using the revenues from those regulated rates to pay site commissions to the correctional facility.¹³⁶

The standard for reviewing whether agency ratemaking is confiscatory is well-settled. “Price control is ‘unconstitutional ... if arbitrary [or] discriminatory.’”¹³⁷ The Court’s focus in reviewing agency ratemaking decisions is whether the regulated rates permit the entity to obtain a return on its investment “sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.”¹³⁸ Adopting regulations that force

¹³³ *Duquesne*, 488 U.S. 299, 307 (1989), citing *Covington & Lexington Turnpike Road Co.*, 164 U.S. 578, 597 (1896).

¹³⁴ *Duquesne*, 488 U.S. at 312.

¹³⁵ *Second FNPRM*, 29 FCC Rcd at 13180 ¶ 21.

¹³⁶ See, e.g., *Securus May 4 ex parte* at 2 (explaining that for Securus “under the Rate Caps, it is economically impossible to continue paying commissions while covering the cost of service and without passing through commissions to end users in the calling rates.”); *GTL April 3 ex parte*) (“To achieve both just and reasonable rates for consumers and fair compensation to ICS providers, the FCC must ensure that reductions in ICS rates and ICS provider proposed changes to ancillary fees are implemented over the same timeframe as site commission reform”).

¹³⁷ *Permian Basin Area Rate Cases*, 390 U.S. 747, 769-770 (1968), quoting *Nebbia v. People of State of New York*, 291 U.S. 502, 539 (1934).

¹³⁸ *FPC v. Hope Nat. Gas Co.*, 320 U.S. 591, 602 (1944).

Marlene H. Dortch
July 21, 2015
Page 26

companies to exit the business are unconstitutional; it is axiomatic that the “power to regulate is not a power to destroy.”¹³⁹

ICS rate caps that do not permit recovery of site commissions would specifically deprive ICS providers of the ability to recover their expenses, including a reasonable return on capital, through the rates they charge for service. The expenses excluded from the FCC’s cost analysis are not insignificant. In some cases they amount to 96% of the revenue ICS providers obtain from serving a particular correctional facility.¹⁴⁰ It is impossible to imagine rational investors willingly lending capital to an enterprise that is subject to rates that prohibit the recovery of such significant costs and is guaranteed to lose money in the process. This is the essence of confiscatory ratemaking.

The FCC’s treatment of site commissions as an “allocation of profit” rather than “costs” in an economic sense will not save its decision. The Supreme Court has made it clear that the review of whether a regulation is confiscatory considers whether the “rate order ‘viewed in its entirety’ ... produce[s] a just and reasonable ‘total effect’ on the regulated business.”¹⁴¹ “It is not the theory but the impact of the rate order which counts.”¹⁴² Therefore, a maximum rate that prevents an ICS provider from charging enough to cover its economic costs plus site commission payments, and still pay some reasonable return to its investors, would be unconstitutional. The FCC cannot rationally separate out the direct costs ICS providers incur to provide service and the expenditures they make on site commissions.¹⁴³ Like the FCC’s rate of return refund rule overturned in *AT&T*, the FCC’s proposed rate caps are impermissible because they “guarantee the regulated compan[ies] an economic loss.”¹⁴⁴

Even if the FCC maintains that site commissions are profit sharing, it must adjust its rate of return prescription to account for the ICS providers’ obligation to make these payments. The D.C. Circuit explained the FCC’s process for setting the rate of return in *AT&T*:

Under the Communications Act ... the [FCC] regulates the rates a carrier may charge for interstate telecommunications service. 47 U.S.C. §§ 201-205 (1982). As part of that task, the [FCC] sets the rate of return on capital that the carrier may use in setting its rates. *See, e.g., Nader v. FCC*, 520

¹³⁹ *Permian Basin*, 390 U.S. at 769, citing *Stone v. Farmers’ Loan & Trust Co.*, 116 U.S. 307, 331 (1886).

¹⁴⁰ *Second FNPRM*, 29 FCC Rcd at 13172 ¶ 3.

¹⁴¹ *Hope Nat. Gas*, 320 U.S. at 602. (internal citations omitted)

¹⁴² *Id.*

¹⁴³ *See AT&T*, 836 F.2d at 1392 (“[i]nvestors in a carrier, after all, must invest in the carrier as a whole ...”).

¹⁴⁴ *Id.* at 1390-91.

F.2d 182, 191-92 (D.C. Cir. 1975) ... The carrier then calculates its rates so that projected revenues will cover projected operating expenses plus the authorized return on capital.¹⁴⁵

Fixing a rate of return requires the FCC to balance investor and consumer interests.¹⁴⁶ The “investor ...has a legitimate concern with the financial integrity of the company whose rates are being regulated ... including that “there be enough revenue ... for operating expenses ...[and] the capital costs of the business.”¹⁴⁷ Under this standard, the return should be “commensurate with returns on investments in other enterprises having corresponding risks.”¹⁴⁸ Further such return “should be sufficient to assure confidence in the financial integrity of the enterprise so as to maintain ...credit and attract capital.”¹⁴⁹

The “commensurate” rate of return for ICS must thus take into account the reduced return available to ICS providers where the correctional facilities are not prohibited from imposing site commissions as a cost of doing business. While the FCC can state that site commission “costs” are not direct costs of providing ICS, it cannot exclude them from its calculation of a reasonable rate of return that is “commensurate” with the risks in other similarly situated enterprises.

The FCC made no such analysis of the rate of return in formulating its interstate ICS rules, and instead relied on the 11.25 percent return assumed in the submitted cost studies, which expressly excluded all site commissions.¹⁵⁰ The FCC must do more than “accept[] the figures in the cost study.”¹⁵¹ It must determine whether the rate of return used in the cost study is sufficient to ensure investor confidence in the business once the rate rules are applied. In determining the appropriate level of ICS rate caps, the FCC must make an independent judgment on whether the cost study developed by parties strikes the appropriate balance between consumers and investors.¹⁵² And unless the rate of return expressly considers the commission payments ICS providers

¹⁴⁵ *Id.* at 1388.

¹⁴⁶ *See Hope Nat. Gas*, 320 U.S. at 603.

¹⁴⁷ *Id.*

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *2013 Inmate Calling Order*, 28 FCC Rcd at 14136, n.203.

¹⁵¹ *Id.*

¹⁵² *See Tex. Office of Pub. Util. Counsel v. FCC*, 265 F.3d 313, 328 (5th Cir. 2001) (rejecting FCC decision to set universal service fund level at \$650 million based solely on consensus of parties below since “agency abdicates its role as a rational decision-maker if it does not exercise its own judgment, and instead cedes near-total deference to private parties’ estimates-even if the parties agree unanimously as to the estimated amount”); *Laclede Gas Co. v. FERC*, 997 F.2d 936, 947 (D.C. Cir. 1993) (FERC was

Marlene H. Dortch
July 21, 2015
Page 28

must make to obtain contracts to provide ICS, the rate of return will fail to strike the appropriate balance and lead to confiscatory rates.

IV. Proposed Solutions

There are a variety of ways the FCC can adopt rules that would limit ICS rates without falling afoul of the problems explored in the preceding sections.

A. Prohibit ICS Providers from Paying Site Commissions

First, the FCC could prohibit ICS providers from paying any site commissions whatsoever, either immediately or after some reasonable transition period (designed to allow them to migrate from existing contracts). Although this action would be within the FCC's legal authority as explained above, it would not necessarily be in the public interest. As many parties have noted in comments, correctional facilities do incur some level of expense to make ICS available to their inmates, and it is in the public interest that this service continue to be available.¹⁵³ It is therefore reasonable for the FCC to permit some level of site commissions, to the extent that facilities are permitted under State law to receive such payments,¹⁵⁴ so that correctional facilities will continue to have an incentive to make adequate ICS facilities available on their premises.

B. Allow ICS Rates to Recover Site Commission Costs Without Limits

Second, at the other extreme, the FCC could adopt no restrictions at all on site commissions, but in that case it would have to allow ICS providers to increase their interstate and intrastate rates to allow them to recover *both* the economic costs of the service, including a reasonable return on investment, *and* the additional economic rent imposed by the site commission obligations. This would be tantamount to having no limits on ICS rates (except in those States that have acted on their own to restrain or prohibit site commissions), since there would be no limits on the payments that correctional facilities could demand, which also would not appear to be consistent with the public interest.

required to exercise independent judgment in approving a settlement even though the figure was within the range pleaded by comments in the agency proceeding below).

¹⁵³ See, e.g., Petro April 20 *ex parte* at 1; GTL April 3 *ex parte*; CenturyLink Reply Comments at 19; Georgia DOC Comments at 17; Praeses Comments at 26.

¹⁵⁴ The FCC should state expressly that it is not pre-empting State and local laws that prevent correctional facilities in some jurisdictions from demanding or receiving commission payments, to avoid any implication that such laws are pre-empted as inconsistent with its regulations under 47 U.S.C. § 276(c).

Marlene H. Dortch
July 21, 2015
Page 29

C. Limits on Site Commissions and Recovery of Costs

Third, the FCC could adopt a middle-ground approach that allows ICS providers to enter into contracts (where permitted by State law) to pay reasonable, but not excessive, site commissions to correctional facilities, and to charge interstate and intrastate rates to their customers that include recovery of these site commission payments in addition to their direct economic costs. As suggested in the undersigned's May 1, 2015, written *ex parte* submission, the FCC should prohibit commission payments computed as a percentage or share of revenue, as these give both correctional facilities and ICS providers a direct incentive to overcharge consumers. The FCC should, however, permit commission payments that are based on minutes of use and similar cost drivers, up to a reasonable maximum. As also suggested in that previous filing, the FCC may prefer to adopt a sliding-scale maximum based on facility size (measured by Average Daily Population), as the record shows that smaller facilities, such as local jails, tend to have disproportionately higher costs than larger ones.¹⁵⁵

If the FCC adopts this approach, though, it is essential that it also adopt a similar sliding-scale maximum rate for interstate and intrastate ICS calls, so that ICS providers will be able to recover the expense of paying site commissions, along with their other costs. It would be particularly difficult for the FCC to justify to a reviewing court a rule that expressly permits ICS providers to pay a certain level of commissions, yet precludes them from recovering these payments from the users of their service. Such a scheme would be internally inconsistent, and therefore almost certainly reversed as arbitrary and capricious.

To ensure that its rules will withstand judicial review, the FCC must adopt a consistent approach that harmonizes rate caps and site commissions. If ICS providers are obligated to pay site commissions, they must be equally entitled to charge rates that will allow them to fulfill that obligation. If the FCC ignores this essential relationship, its laudable efforts to rein in ICS rates will be doomed to fail.

1. Legal Basis

It is well-established that the FCC has broad discretion in establishing just and reasonable rates, as long as it articulates a rational basis for its decisions and as long as the result is not confiscatory. As the Supreme Court has explained in construing the similar "just and reasonable rates" provision of the Natural Gas Act, the agency

¹⁵⁵ Nonetheless, the mere designation of a facility as a jail rather than a prison, by itself, does not indicate much about its likely costs. Some jails, for example, house state prisoners under long-term contracts and therefore have cost patterns that more closely resemble those of prisons. *See Reply Comments of Petitioners Martha Wright et al.* at 15-16 (filed Jan. 13, 2014).

Marlene H. Dortch
July 21, 2015
Page 30

... is not required by the Constitution or the Natural Gas Act to adopt as just and reasonable any particular rate level; rather, courts are without authority to set aside any rate selected by the Commission which is within a “zone of reasonableness.”“ *FPC v. Natural Gas Pipeline Co.*, 315 U. S. 575, 585. No other rule would be consonant with the broad responsibilities given to the Commission by Congress; it must be free, within the limitations imposed by pertinent constitutional and statutory commands, to devise methods of regulation capable of equitably reconciling diverse and conflicting interests.¹⁵⁶

Thus, for example, FCC is not required to impose the same maximum rate of return on all types of carriers, or even on all carriers of the same class. This is amply demonstrated by the adoption of price cap rules for local exchange carriers, under which a carrier that succeeds in operating its business more efficiently may achieve a higher rate of return than others that fail to realize similar efficiency.¹⁵⁷ The FCC found that the public interest benefits of creating economic incentives for carriers to reduce their costs justified the departure from its historic practice of strict rate-of-return regulation.¹⁵⁸

Also, importantly, FCC may base ratemaking decisions on surrogates and even “reasoned guesswork,” if informed by its “historical experience and expertise,” in the absence of specific, reliable data.¹⁵⁹ In that case, FCC had adopted a \$25 access surcharge on private lines that could “leak” interstate traffic to the public network, so that users of these lines would contribute something to the cost of the interstate network. The FCC was unable to obtain reliable data concerning the volume of leaked traffic, but decided to impose an interim rate of \$25 as a surrogate until more accurate data could be compiled. The Court of Appeals, on review, found this approach reasonable, and rejected arguments that FCC had the burden of providing a more specific cost justification for its rate prescription. “It is not the FCC’s chore to convince us that what it has done is the best that could be done, but that what it has done is reasonable under

¹⁵⁶ *Permian Basin*, 390 U.S. at 767; see also *Verizon Communications Inc. v. FCC*, 535 US 467, 501-02 (2002) (citing *Permian Basin* as guidance for interpretation of Telecommunications Act of 1996); *National Ass’n of Reg. Util. Com’rs v. FCC*, 737 F.2d 1095, 1141 (D.C. Cir. 1984) (“NARUC”) (citing *Permian Basin* in upholding the FCC’s adoption of \$25 special access surcharge).

¹⁵⁷ *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786, 6789 ¶ 22 (1990) (subsequent history omitted).

¹⁵⁸ *Id.* at 6787 ¶ 2; see *Nat’l Rural Telecomm. Ass’n v. FCC*, 988 F.2d 174, 183-85 (D.C. Cir. 1993) (rejecting as “complete *non sequitur*” MCI’s argument that price cap earnings sharing rule was arbitrary because it “does not retain as much of rate-of-return regulation” as would have another proposal).

¹⁵⁹ *NARUC*, 737 F.2d at 1140-41.

Marlene H. Dortch
July 21, 2015
Page 31

difficult circumstances. Here the unique nature of an unmeasurable but real problem of hidden access assists the FCC in justifying what it has ordered.”¹⁶⁰

In this case, the FCC faces a problem similar in some respects to that confronted in the *NARUC* decision. The record shows clearly that correctional facilities incur some costs to make ICS available to their inmates, but (as discussed further in the following section) the evidence is far less clear as to the amount of those costs. Furthermore, the entities incurring the costs (typically sheriffs and prison systems) are not themselves offering regulated communications services, are not subject to FCC’s direct jurisdiction, and have no uniform system of accounting for ICS-related costs. It will therefore be difficult and resource-intensive for the FCC to obtain reliable cost information, if it is possible at all; and such information would then require constant updating and revision to keep it current. This is precisely the type of situation in which the use of reasonable surrogates is not only permissible, but desirable, to avoid placing substantial new compliance burdens on correctional institutions that wish to continue receiving site commission payments.

Besides the private line surcharge discussed above, the FCC has used surrogates, proxies and formulae in lieu of actual cost data in other contexts. In administering the Universal Service program, for example, FCC established a reimbursement formula for schools and libraries that relied on surrogate data to estimate each recipient’s level of need, rather than performing site-specific analyses that would have been administratively infeasible.¹⁶¹ Also, the FCC decided to base high-cost reimbursement for larger ILECs on forward-looking cost models that estimate costs for specific locations based on mathematical formulae, recognizing that conducting a separate cost study for each particular location would be entirely impracticable.¹⁶² For smaller ILECs, the FCC has adopted a formula to limit the corporate operations expenses recoverable from the high cost fund, as a more feasible alternative to conducting company-specific investigations of the reasonableness of such expenses.¹⁶³

¹⁶⁰ *Id.* at 1141.

¹⁶¹ See *Letter to Mel Blackwell, Vice President Schools and Libraries Division, USAC, from Trent B. Harkrader, Chief, Telecommunications Access Policy Division, Wireline Competition Bureau*, 27 FCC Rcd 8860 (Wireline Comp. Bur. 2012).

¹⁶² See *Connect America Fund; High-Cost Universal Service Support*, Report and Order, 28 FCC Rcd 5301 ¶ 1 (Wireline Comp. Bur. 2013); *Connect America Fund et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 17734 ¶ 184 (2011) (“*USF/ICC Transformation Order*”) *aff’d* 753 F.3d 1015 (10th Cir. 2014), *cert denied. United States Cellular Corp. v. FCC*, Case 14-610 et al. (May 4, 2015); *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776, 8888-89, ¶¶ 199, 203 (1997).

¹⁶³ See *USF/ICC Transformation Order*, 26 FCC Rcd at 17747-48 ¶ 229-232.

Marlene H. Dortch
July 21, 2015
Page 32

Moreover, the fact that the FCC treats site commission payments as an allocation of profit, rather than as a cost of service, has no bearing on its ability to adopt a sliding-scale formula to limit such payments. The FCC has ample statutory discretion to determine the level of “profit” that can be included in a just and reasonable rate. As already noted, it has effectively allowed for a wide range of potential earnings in adopting incentive regulation for large ILECs. It can similarly allow for a range of earnings, albeit with more constraints, by permitting a range of site commission payments based on the size of the facility.¹⁶⁴

Similarly, for purposes of determining whether maximum rates are confiscatory, in violation of the Fifth Amendment, it does not matter whether the FCC considers site commissions as “costs” or as “profits.” The Supreme Court has made it clear that the review of whether a regulation is confiscatory considers whether the “rate order ‘viewed in its entirety’ ... produce[s] a just and reasonable ‘total effect’ on the regulated business.”¹⁶⁵ “It is not the theory but the impact of the rate order which counts.”¹⁶⁶ Therefore, a maximum rate that prevents an ICS provider from charging enough to cover its economic costs plus site commission payments, and still pay some reasonable return to its investors, would be unconstitutional.¹⁶⁷

Accordingly, it would be both reasonable and proper for the FCC to adopt a formula approach to determining the maximum reasonable site commission payment for ICS providers, instead of going down the burdensome and potentially endless path of trying to analyze costs on a site-by-site basis. This provides an administratively feasible and flexible method of capping site commissions, and if experience proves that the cap results in a reduction in the availability of telephones to inmates (or, conversely, results in unreasonably high rates for ICS calls), FCC would be able to adjust the formula.

Considering the record evidence, including the studies submitted by GTL and other parties, the undersigned suggests that FCC should find that agreeing to pay site commissions in excess of the following levels is an unreasonable practice by ICS providers:

¹⁶⁴ State regulatory agencies operating under similar statutory authority have, for example, sometimes allowed some regulated companies to earn higher rates of return than others as a reward for good management or for undertaking particular investments that served the public interest. *See, e.g., Pa. Pub. Util. Comm’n v. PPL Elec. Utils. Corp.*, R-2012-2290597, Order at 93-98 (Pa. Pub. Util. Comm’n 2012).

¹⁶⁵ *Hope Natural Gas*, 320 U.S. at 602 (1944) (internal citations omitted).

¹⁶⁶ *Id.*

¹⁶⁷ *See also Duquesne*, 488 U.S. at 307.

Marlene H. Dortch
July 21, 2015
Page 33

Average Daily Population (ADP) of Facility	Maximum per minute
1,000 or greater	\$0.01
300 to 999	\$0.02
Below 300	\$0.03

Conversely, if an ICS provider agrees to pay site commissions that do not exceed these levels, it should be permitted to increase its rates by an amount equal to the required payments under its agreement.¹⁶⁸

There are no practical alternatives to this approach in the record. No party has seriously suggested that the FCC should, or even could, attempt to make site-by-site cost determinations, either through rulemaking or through individualized waiver proceedings. Either of these approaches would be unreasonably wasteful of both parties' and the FCC's limited resources. The only other possibilities would be to prohibit site commission payments entirely, or else to leave them completely unrestricted (as they were before the first Report and Order in this docket). The former, although within the scope of the FCC's authority,¹⁶⁹ appears likely to lead to results contrary to the public interest, as it could lead some correctional facilities to reduce or eliminate inmate access to phones. The latter would simply reinstate the principal cause of the unreasonable ICS rates that led the FCC to act in the first place.¹⁷⁰ As the record amply shows, in the absence of any regulatory constraint, site commissions were not related in any way to cost, nor were they restrained by any market forces. ICS providers had an incentive to offer increased site commissions, not to restrain them, as a way of getting access to more facilities; and consumers had no influence at all on the negotiation of these commissions, even though this expense was being passed through to them in rates for calls. Therefore, there is no alternative to adopting a cap on site commissions based on a surrogate formula that would be both feasible to administer and consistent with the FCC's public interest goals.

2. Costs Claimed by Correctional Institutions Are Excessive

Numerous filings have been submitted by correctional facilities and associations claiming they need site commissions to recover their cost of allowing ICS. Only a fraction of those entities

¹⁶⁸ See Lipman May 1 *ex parte* at 6; Lipman June 1 *ex parte* at 18-19. This approach allows individual States to impose their own regulations limiting or prohibiting site commissions, since it merely permits but does not require ICS providers to enter into agreements to pay site commissions, and the FCC should announce expressly that any such State regulations are not inconsistent with its rules.

¹⁶⁹ Lipman June 1 *ex parte* at 9-12 (discussing FCC authority under sections 276 and 4(i) among others); Lipman April 8 *ex parte* at 1-7 discussing FCC authority under sections 201, 276, and 4(i) of the Act).

¹⁷⁰ Lipman June 1 *ex parte* at 3, 5; Lipman April 8 *ex parte* at 2-3.

Marlene H. Dortch
July 21, 2015
Page 34

submitting such filings, however, produced any cost data to buttress their claims. As described below, none of the few entities that provided cost data sufficiently explained and documented their data inputs and cost allocation methodologies or produced work papers to evaluate their analysis. All of the submissions lack the kind of detail that would be required in a rate proceeding to justify their accuracy and are deficient as compared with ICS providers' detailed cost analysis supported by expert economist reports.

The FCC can reject the broad unsupported claims of the correctional facilities and associations because relying on them would be arbitrary and capricious decision making. The agency cannot rely on data or cost methodologies submitted in the record “without ascertaining the accuracy of the data contained in the study or the methodology used to collect the data.”¹⁷¹ Such a decision would be “arbitrary agency action, and the findings based on [such a] study are unsupported by substantial evidence.”¹⁷² In other words, it is error for the FCC to rely on cost data that have “no explanation or underlying support.”¹⁷³

As a general rule, the FCC requires sufficient detail about the methodology, calculations, assumptions, and other data used to develop submitted costs.¹⁷⁴ Such detail is necessary to provide the capability to examine and modify the critical assumptions and to ensure transparency.¹⁷⁵ That is, the logic and algorithms should be “revealed, understandable, capable of being adjusted by the parties and regulators, and not contain ‘black boxes.’”¹⁷⁶ Submissions that lack sufficient detail to evaluate claimed costs are typically rejected by the FCC.¹⁷⁷ A submission, for example,

¹⁷¹ *City of New Orleans v. SEC*, 969 F.2d 1163, 1167 (D.C. Cir. 1992).

¹⁷² *Home Health Care, Inc. v. Heckler*, 717 F.2d 587, 592 (D.C. Cir. 1983) (footnote omitted); cf. *Ohio Bell Tel. Co. v. Public Utils. Comm'n*, 301 U.S. 292, 303 (1937) (“[H]ow was it possible for the appellate court to review the law and the facts and intelligently decide that the findings of the FCC were supported by the evidence when the evidence that it approved was unknown and unknowable?”).

¹⁷³ *City of New Orleans v. SEC*, 969 F.2d at 1167.

¹⁷⁴ *Federal-State Joint Board on Universal Service et al.*, Tenth Report and Order, 14 FCC Rcd 20156, 20205 ¶ 107 (1999).

¹⁷⁵ *Universal Service First Report and Order*, Report and Order, 12 FCC Rcd 8776, 8915 ¶ 250 (1997) (setting forth criteria for forward-looking cost methodologies).

¹⁷⁶ *Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc.*, Memorandum Opinion and Order, 18 FCC Rcd 17722, 17747 ¶ 48 (2003).

¹⁷⁷ See, e.g., *Broward County, Florida and Sprint Nextel Corporation Mediation No. TAM-50073*, Memorandum Opinion and Order, 26 FCC Rcd 7635, 7647 ¶¶ 44-45 (2011) (rejecting requested spectrum relocation costs for failing to provide justification such as what work the costs would cover); *WTVG, Inc., Petition for Waiver of Section 76.92(f) of the FCC's Rules*, Memorandum Opinion and Order, 25 FCC Rcd 2665, 2676, ¶ 19 (2010) (rejecting a cable operator's costs analysis to stop carrying a duplicate

Marlene H. Dortch
July 21, 2015
Page 35

that summarizes results and does not disclose the inputs used cannot be replicated or confirmed and therefore may be refused.¹⁷⁸

The FCC can determine the types of costs that are allowable or disallowed as being caused directly by the provision of ICS. The “used and useful” standard provides the foundation of FCC decisions evaluating whether particular investments can be included in a carrier’s revenue requirement. Property, for example, is considered “used and useful” for regulatory ratemaking if it is “necessary to the efficient conduct of a utility’s business, presently or within a reasonable future period.”¹⁷⁹ The FCC has investigated and invalidated access rates when the carrier failed to demonstrate an increase in operating expenses and an excessive rate of return.¹⁸⁰ The FCC has also prohibited a business from including goodwill or other intangible costs.¹⁸¹

The FCC has identified general principles regarding what constitutes “used and useful” but has recognized “that these guidelines are general and subject to modification, addition or deletion. The particular facts of each case must be ascertained in order to determine what part of a utility’s investment is used or useful.”¹⁸² One is the equitable principle that ratepayers should not be forced to pay a return except on investments that can be shown to benefit them.¹⁸³ The FCC considered this equitable principle when it determined a portion of the cost of a video cable, not

station because it merely introduced a laundry list of costs); *Numbering Resource Optimization et al.*, Second Report and Order, Order on Reconsideration in CC Docket No. 96-98 and CC Docket No. 99-200, and Second Further Notice of Proposed Rulemaking in CC Docket No. 99-200, 16 FCC Rcd 306, 379 ¶ 182 (2000) (finding amount and detail of data insufficient to determine shared industry and direct carrier-specific costs of thousands-block number pooling); *Petition of Pacific Bell Telephone Company Under Section 69.4(g)(1)(ii) of the FCC’s Rules for Establishment of New Service Rate Elements*, Memorandum Opinion and Order, 13 FCC Rcd 6545, 6549 ¶ 9 (1998) (suspending tariff revisions for failing to provide sufficient cost justification and other support to permit a full assessment of the reasonableness of the proposed charges and rate structures).

¹⁷⁸ See *Access Charge Reform (CALLS II Order)*, Order, 17 FCC Rcd 10868, 10882-84 ¶¶ 33-36 (2002) (refusing to use carrier cost studies that summarize results because it is impossible to replicate or confirm the results without disclosing the inputs used).

¹⁷⁹ *Sandwich Isles Communications, Inc. Petition for Declaratory Ruling*, Opinion, 25 FCC Rcd 13647, ¶ 12 (2010) (“*Sandwich Isles*”) (citing *American Tel. and Tel. Co.*, Phase II Final Decision and Order, 64 FCC 2d, at 38, para. 111 (1997) (*AT&T Phase II Order*)).

¹⁸⁰ See *Beehive Tel. Co., Inc., Tariff FCC No. 1*, Memorandum Opinion and Order, 13 FCC Rcd 2736 (1998), *modified on recon.*, 13 FCC Rcd 11795 (1998), *aff’d*, *Beehive Tel. Co., Inc. v. FCC*, 180 F.3d 314 (1999).

¹⁸¹ *Implementation of Sections of the Cable Television Consumer Protection & Competition Act of 1992: Rate Regulation*, 11 FCC Rcd 2220, 2239 ¶ 42 (1996).

¹⁸² *Sandwich Isles*, 25 FCC Rcd at 13651 ¶ 12.

¹⁸³ *Id.* at 13652.

Marlene H. Dortch
July 21, 2015
Page 36

then being used to provide video service, was partially eligible for inclusion in the rate base.¹⁸⁴ “In balancing the equities between the interests of carriers and rate payers, the FCC found that ‘video service customers have benefitted to some degree from [the] decision to include [polyethylene shielded video] cable in composite sheaths.’”¹⁸⁵

None of the correctional facilities and associations submitted sufficient detail in this proceeding either to support the amount of their alleged costs, or to demonstrate that these costs meet the used and useful standard. In fact, many correctional facilities misleadingly claim to be entitled to payment for activities that have nothing to do with the provision of a telecommunications service. They improperly identify several activities, such as surveillance and investigation of calls, that are basic law enforcement activities and not costs for providing a telecommunications service. Correctional facilities typically monitor or supervise *all* communications between inmates and outside parties, such as mail and in-person visits, as part of their internal security function. Likewise, if inmates commit crimes or violate prison rules while communicating in person or by mail, the correctional facility will incur costs to investigate and prosecute these offenses. These functions are part of the general duties of law enforcement, regardless of the medium of communication used, and the cost of these functions is part of the cost of operating a correctional facility, not a cost to be borne by the recipient of a letter, the prison visitor, or the other party to a telephone call.

As another commenter pointed out, the funding of law enforcement activities “is the responsibility of government ... [not] telecommunications costs that should be paid from ICS rate revenue.”¹⁸⁶ The use of an ICS security tool by an investigator to secure a conviction or spot illegal activity that happens to involve the use of a telephone does not transform their time into an ICS cost, and such costs should be paid by governments if they help investigators to perform their job.¹⁸⁷ Correctional facilities must supervise inmate movements at all times, and supervising movements to make a telephone call does not make such expense an ICS cost as opposed to a general operating cost.¹⁸⁸ Costs for free calls that are statutorily required are not an ICS cost but attributable to external legal requirements that should be funded by general revenues.¹⁸⁹ To the extent that correctional facilities handle inquiries from the U.S. Marshals, those costs should be

¹⁸⁴ See *Investigation of Special Access Tariffs of Local Exchange Carriers*, FCC 86-52 (1985), *re-manded on other grounds*, *MCI Telecom. Corp. v. FCC*, 842 F.2d 1296 (D.C. Cir. 1988).

¹⁸⁵ *Sandwich Isles*, 25 FCC Rcd at 13653 ¶ 14.

¹⁸⁶ See Prison Policy Initiative Reply Comments at 7 (filed Jan. 27, 2015). (“Prison Policy Initiative Reply Comments”).

¹⁸⁷ *Id.*

¹⁸⁸ *Id.* at 9.

¹⁸⁹ *Id.* at 8.

Marlene H. Dortch
July 21, 2015
Page 37

recouped under contracts with the U.S. Marshals and not site commissions.¹⁹⁰ Simply put, all of the aforementioned activities are part of the general duties of law enforcement and are not directly related to the provision of ICS.

Several commenters likewise inappropriately identify educational and welfare costs. These programs may be beneficial to society but they are not telecommunications services and telecommunications consumers should not have the responsibility to pay for them.¹⁹¹ As the FCC acknowledged, “the Act does not provide a mechanism for funding social welfare programs or other costs unrelated to the provision of ICS, no matter how successful or worthy.”¹⁹² Yet, in 2013, “ICS users and their families, friends and lawyers spent over \$460 million to pay for programs ranging from inmate welfare to roads to correction facilities’ staff salaries to the state or county’s general budget ... [which] appears to be of limited relative importance to the combined budgets of correctional facilities [but] has life-altering impacts on prisoners and their families.”¹⁹³ These individuals should not have to disproportionately bear the costs for educational and welfare programs. The costs should be paid for from general revenue sources because reducing recidivism and providing basic care are core responsibilities of the correctional facilities and the governments that imprisoned the offenders.¹⁹⁴ The FCC also should not be swayed by spurious arguments that educational and welfare programs will be eliminated without site commissions. States like New York banned ICS commissions and still managed to obtain funding from other resources to continue beneficial educational and welfare programs.¹⁹⁵

The undersigned responds below to many of the cost assertions and data submitted by correctional facilities and associations. In short, most of the correctional facilities have not documented costs that are actually caused by the provision of ICS and have provided only unverified and undocumented assertions without sufficient detail about the methodology, calculations, assumptions, and other data to evaluate and validate cost information.

The National Sheriffs’ Association (“NSA”) asserts that every jail incurs costs for officers’ time to maintain security and administer the ICS system and provides some information from a survey it conducted of its 3,000 members regarding the amount of time spent on security and administrative duties in connection with ICS.¹⁹⁶ The FCC should reject this survey as inconclusive given

¹⁹⁰ *Id.*

¹⁹¹ See Letter from Andrew Lipman to Marlene H. Dortch (filed Feb. 20, 2015).

¹⁹² *2013 Inmate Calling Order*, 28 FCC Rcd 14138 at ¶ 57.

¹⁹³ *Second FNPRM*, 29 FCC Rcd at 13181 ¶ 23.

¹⁹⁴ See Prison Policy Initiative Reply Comments at p. 3.

¹⁹⁵ See Human Rights Defense Center Reply Comments at 3 (filed Jan. 27, 2015). (“HRDC Reply Comments”)

¹⁹⁶ Comments of The National Sheriffs’ Association (filed Jan. 12, 2015).

Marlene H. Dortch
July 21, 2015
Page 38

that only 5% of NSA's members (about 152) responded (and there is no analysis of whether these respondents constitute a representative sample of the membership), only "the most recent three months of data" were used, and no calculations were provided of average costs and standard deviation. The submission should also be rejected because it does not provide sufficient details to validate the result. Specifically, NSA does not separately identify the costs for each task and instead separates information into two broad categories (administrative and security) and by employee type (e.g., officer, supervisor and other). NSA does not specifically explain what may be encompassed by "other duties" in the two categories or "other" type of employee. NSA does not explain the methodology for allocating time between various tasks and categories, particularly any shared time and costs. NSA also did not produce a copy of the survey or any work papers.

NSA also claims that ICS revenues are needed for trained officers to "daily monitor and review information to protect the public from abuse and prevent criminal activity." However, as explained above, these are basic law enforcement activities that have nothing to do provision of ICS. Thus, the FCC should decline to include any basic law enforcement activity as a cost for providing ICS.

NSA argues that the above criticism of NSA's incomplete and methodologically unsound cost analysis is inappropriate because, "as unregulated entities, Sheriffs are not required to keep data in the same format as entities regulated by FCC. Sheriffs and jails also do not have staffs that include attorneys, accountants and economists schooled in the art of ratemaking principles and [FCC] rules and regulations on cost studies."¹⁹⁷ The undersigned agrees. This is one of the reasons that it would be infeasible for FCC to try to apply traditional regulatory tools to determine precise economic costs of offering telephone service in correctional facilities. As noted in earlier,¹⁹⁸ correctional facilities are not operated as for-profit businesses, so it stands to reason that they cannot be expected to generate the same type of cost information that a private business would. The FCC should instead adopt a more practical and readily administrable approach using a simple formula to estimate the maximum reasonable commission payment, as urged by both NSA and the undersigned.

NSA also disputes the undersigned's criticisms of its cost analysis. To some extent, NSA acknowledges the criticisms are accurate but contends they do not matter. For example, it acknowledges that its study was based on only three months of usage data, but contends that this is "sufficient" and that FCC can gather more data if it needs it.¹⁹⁹ It also concedes that most sheriffs did not identify costs for specific tasks, so that NSA was unable to provide this level of

¹⁹⁷ Letter from Mary J. Sisak, Counsel to The National Sheriff's Association to Marlene H. Dortch, FCC at 6 (filed June 12, 2015) ("NSA Letter").

¹⁹⁸ Lipman May 1 *ex parte*, at 2.

¹⁹⁹ NSA Letter at 6.

Marlene H. Dortch
July 21, 2015
Page 39

detail in its results.²⁰⁰ The undersigned submits that these admissions by NSA simply confirm that its cost study is not a reliable basis for estimating those costs relevant to FCC's statutory task of determining "fair" compensation. Other assertions are unsupported and unverifiable. Notably, NSA contends that its survey respondents "are a *representative sample* of jails of different sizes and in different states"²⁰¹ In fact, however, only about 5% of NSA's members responded to its survey, and there is no data from which one could determine whether these relatively few respondents are representative of the rest of the membership.²⁰² There is good reason to suspect the opposite, since those sheriffs with relatively low costs would have had less motivation to respond to the survey than those with relatively high costs. NSA admits, in particular, that it received a response from only *one* jail with an ADP over 2,500,²⁰³ rendering its cost estimate for this category especially suspect.

NSA's arguments are largely echoed in the May 8 *ex parte* submitted on behalf of Pay Tel Communications.²⁰⁴ Like NSA, Pay Tel argues that the cost data collected by NSA is "robust" based on the number of sheriffs surveyed, without any analysis of whether or not this self-selected sample is representative of the overall population of jails.²⁰⁵ Pay Tel also argues that all functions performed by jail personnel that relate in any way to ICS must be treated as direct costs of ICS, because "they would not be required *but for* the availability of ICS[.]"²⁰⁶ This is a simplistic analysis. One could just as easily conclude that if a jail provides chess boards for its inmates to use in a recreation facility, the cost of playing chess includes the salaries of the officers who attend to the recreation room, because those officers would not be needed if the inmates were not permitted to play chess. It is obvious that any activity conducted in a correctional facility costs much more than doing the same thing in the "outside" world; no one needs elaborate studies or economic analyses to prove this. But that does not make it sound public policy to shift the costs of those activities to the families and friends of inmates, as the sheriffs seek to shift the costs of telephone service to those who wish to receive calls from inmates.

²⁰⁰ NSA Letter at 7.

²⁰¹ NSA Letter at 6 (emphasis supplied.)

²⁰² Lipman April 8 *ex parte* at 11. Ironically, *more* sheriffs' offices and associations have filed comments or *ex parte* letters in this docket (214), according to the FCC's Electronic Comment Filing System, than responded to NSA's cost questionnaire (152).

²⁰³ NSA Letter at 3.

²⁰⁴ Letter from Timothy G. Nelson to Marlene H. Dortch, May 8, 2015 ("Pay Tel Letter").

²⁰⁵ Pay Tel Letter at 4-5.

²⁰⁶ Pay Tel Letter at 5 (emphasis in original).

Marlene H. Dortch
July 21, 2015
Page 40

Praeses LLC claims that a survey of its Correctional Clients demonstrates an average cost per minute of \$0.18 (and \$1.88 per call and \$34.46 per inmate) with a standard deviation of \$0.12.²⁰⁷ However, Praeses admits the raw data demonstrated “dramatic disparity” because different parties may include different types of costs and/or measure and prorate costs in different ways, resulting in non-standardized cost information.²⁰⁸ The FCC should therefore reject this survey. Praeses did not disclose how many correctional facilities responded or what period of time was used by the various respondents. Also, although Praeses provided a sample copy of the survey, it did not provide any work papers and did not explain or document its methodology for using the raw data to calculate the average costs and standard deviations.

Cook County, Illinois indicates that it receives \$2.4 million annually (which is approximately equivalent to \$0.08 per minute) to perform a wide variety of tasks related to ICS operation, which are comprised of managing the contract and monitoring provider performance (\$138,000); enrolling new detainees into the ICS system (\$114,000); resetting or re-enrolling detainees in its voice biometric system (\$710,000); monitoring calls and retrieving/copying call recordings (\$362,000);²⁰⁹ administrating a debit card program (\$441,000); and inspecting phones, responding to telephone-related grievances, and facilitating phone maintenance (\$318,000).²¹⁰ While this report provides some details about staffing salaries, benefits, and hours spent on each task, its cost information is far less comprehensive than the studies filed by ICS providers. For example, the ICS provider cost studies separately identify types of costs (e.g., direct costs, shared costs) and describe the step-by-step process to categorize and allocate costs, including a break-down of site commissions between local, intra-LATA, inter-LATA, interstate, and international services. The ICS provider cost studies determine standard deviations and address items that can affect cost averages like unpredictable call volume. They also identify who conducted the analysis and his or her qualifications do so. Cook County did not provide this level of detail.

Cook County’s study demonstrates the potential for operators to inflate their cost claims in the absence of any standard form of cost documentation and any third-party scrutiny of cost data. Cook County states that it operates “one of the largest single-site county confinement facilities in the nation,” with an average daily population (ADP) of 9,000 inmates,²¹¹ so it might be expected to realize some economies of scale relative to smaller facilities. Yet its study estimates annual costs of \$2.4 million, or \$0.08 per minute, which is far above the range of GTL’s study. A review of the study suggests several possible reasons for this discrepancy:

²⁰⁷ Praeses Comments at 35.

²⁰⁸ *Id.* at 35-36.

²⁰⁹ As noted above, monitoring and recording calls is properly a general law enforcement function, since the facility is required to monitor all inmate communications regardless of the medium.

²¹⁰ Comments of Cook County, Illinois (filed Jan. 12, 2015) (hereinafter “Cook County”).

²¹¹ *Id.* at 1.

- The study includes \$362,000 in call monitoring costs, including among other things responding to subpoenas for call records.²¹² As discussed above, call monitoring is not properly a cost of providing ICS, but a cost of securing the correctional facility, and responding to subpoenas for call records is an operational cost not unlike responding to subpoenas for any other records relating to an inmate.
- The largest single item, by far, is \$710,000 for “voice biometric resets & re-enrollments.” The study indicates that the re-enrollment process is similar to initial enrollment (for which the reported cost is only \$114,000), but also includes an investigation to determine whether re-enrollment is necessary followed by transporting the detainee to a telephone.²¹³ The time allotted for initial enrollments is 2 minutes, but the time allotted for re-enrollments ranges from 7.3 minutes to 16.8 minutes, varying by division.²¹⁴ There is no explanation of why the jail counts the time required to transport a detainee to the re-enrollment telephone as a cost of ICS, when it (properly) does not count as a cost the time its officers necessarily spend monitoring detainees when they are going to or from a telephone to make calls. Further, the jail allocates up to five persons (four correctional officers and one sergeant, with the number varying by division) to *each* re-enrollment.²¹⁵ The highest personnel total is for Division 9, which is the jail’s “super-maximum” security division.²¹⁶ Although undoubtedly this division is more costly to operate than other divisions due to its higher security requirements, these additional costs are not caused by the provision of ICS, but rather are caused by the characteristics of the inmates assigned to this division. Correctional facilities should not be permitted to assign the costs of general facility security requirements, no matter how necessary or appropriate these costs may be to the performance of their custodial functions, to customers of ICS.
- Cook County allocates 3.7 FTEs (\$318,000) to telephone inspections, and 4.2 FTEs (\$363,000) to telephone maintenance. Telephone inspection reportedly consumes anywhere from 4 minutes per shift to 86 minutes per shift (2 shifts per day), varying by divi-

²¹² *Id.* at 4.

²¹³ *Id.* at 4.

²¹⁴ *Id.*, attachment at 2-3.

²¹⁵ *Id.* For example, for Division 1, Cook County estimates that it performs 23 re-enrollments per week at 15.1 minutes per enrollment; this comes to a total of 18,059 minutes or 300 hours per year. The county allocates a total of 1,728 hours per full-time employee per year (*id.* attachment at 5), so 300 hours is about 0.17 FTE. But Cook County assigns 0.7 FTE to Division 1 for this function, for three correctional officers and one sergeant, implying that all four of these personnel are being assigned to this task for its full duration (including the preliminary investigation to determine whether a re-enrollment is warranted).

²¹⁶ http://www.cookcountysheriff.com/doc/doc_DivisionsOfJail.html (visited Apr. 29, 2015).

Marlene H. Dortch
July 21, 2015
Page 42

sion.²¹⁷ Although, as already noted, Cook County's jail facility is one of the nation's largest, it still strains credulity to assert that telephone inspection requires nearly three hours per day, seven days a week, in Division 2, or that this task requires the equivalent of nearly four full-time positions (which, since there are two shifts, would imply that two correctional officers are inspecting telephones somewhere in the jail during every minute of every shift). These totals indicate either a flawed cost study methodology or inflated cost allocations. Similarly, the amounts allocated to telephone maintenance appear excessive, especially considering that the county's ICS vendor actually performs the maintenance.²¹⁸

- The County reports costs of \$441,000 annually, or 5.1 FTEs, for managing its pre-paid telephone debit card system. According to the cost study, four correctional officers spend 16 hours per week *each* "sorting and packaging" debit cards, and *another* 16 hours per week *each* on "delivery."²¹⁹ These two functions consume about three-fourths of the costs assigned to this category. The county states that it processes 1,900 debit cards weekly;²²⁰ thus, it is allowing a full two minutes for "sorting and packaging" each individual card, and another two minutes for delivery. These figures suggest either a highly inefficient method of operating this program, or (again) a flawed cost study methodology.
- The items listed above account for at least 80% of the total cost claimed by the Cook County study. Given the pervasive problems identified in these sections of the study, it is possible that other costs are also overstated, but these have not been examined due to their relatively smaller amounts.

Approximately 12 California sheriffs describe a California law that requires all commission proceeds to be deposited into inmate welfare funds ("IWFs") and list numerous educational and welfare programs paid for by the IWFs such as substance abuse education and treatment programs, re-entry services, vocational programs, life skills, counseling, legal research, religious services and ministry, enhanced medical services, hygiene items, books, newspapers, board games, playing cards, exercise equipment, televisions and television service.²²¹ However, the

²¹⁷ Cook County, attachment at 4.

²¹⁸ Cook County at 5 ("the ICS provider's staff ... repairs the equipment under guard and escort by CCSO staff.") Escorting the telephone maintenance staff is a general security function of the jail, like escorts for any other contractor or outside personnel who might need to perform tasks inside the facility, and should not be charged to ICS customers.

²¹⁹ Cook County, attachment at 3.

²²⁰ Cook County at 4.

²²¹ Alameda County, CA Sheriff's Office Comments (filed Jan. 16, 2015); Imperial County, CA Sheriff Comments (filed Dec. 30, 2014); Kern County, CA Sheriff's Office Comments (filed Jan. 5,

Marlene H. Dortch
July 21, 2015
Page 43

California law merely requires any such proceeds to be deposited into welfare funds *if* collected, and does not require the collection of site commissions. These California sheriffs make no attempt to explain how these educational and welfare programs are connected to the provision of ICS or why they should be paid for by telecommunications consumers rather than as part of the general prison budget.

The California sheriffs also do not provide justification for their IWF or other costs. Several simply declare an overall budget or expected impact. For example, the Orange County Sheriff states the FCC proposal would reduce its IWF by 70% or \$4.3 million. The Kern County Sheriff states almost 50% of its IWF budget of \$3.9 million is generated from ICS commissions of \$1.8 million annually. The Alameda County Sheriff states \$8.5 million is spent to support IWF and removal of commissions and in-kind payments would reduce and/or eliminate the programs and services. Shasta County Sheriff states phone commissions fund nearly \$240,000 of inmate programs and services.

Similarly, San Francisco claims it spent about \$1.1 million of IWF amounts for staffing (\$572,606); recidivism reduction programming (\$381,453); and inmate services and supplies (\$180,599), but does not describe how these costs relate to ICS or provide any justification for the costs. The Los Angeles County Sheriff estimates a \$6 million annual cost to service and maintain the ICS system, including investigatory actions, but provides no specifics about the tasks that comprise that estimate. Another commenter submitted a copy of the Los Angeles County IWF expense account, which includes a variety of costs including clothing and personal supplies; food; household expenses; and medical, dental and lab supplies,²²² and highlighted inconsistencies between the use of IWF funds by Los Angeles County and information submitted by San Francisco stating that IWF amounts cannot be used for meals, clothing, housing or medical services.²²³

Imperial County Sheriff estimates that its operational expenses for ICS are \$215,000 a year or \$0.34 per minute. It produced certain employee salary and hour information used to calculate the estimate but does not explain the tasks connected to provision of ICS, how costs might be prorated or shared, or the methodology for assigning hours. It also claimed that “monitoring,

2015); Los Angeles County, CA Comments (filed Jan. 9, 2015) Orange County, CA Sheriff Comments (filed Jan. 6, 2015); Riverside County, CA Sheriff Comments (filed Dec. 30, 2014); San Bernardino County, CA Sheriff’s Department Comments (filed Nov. 24, 2014); San Diego County, CA Sheriff’s Department Comments (filed Jan. 26, 2015); San Francisco City and County, CA Sheriff’s Department Comments (filed Dec. 15, 2014); Santa Barbara County, CA Sheriff Comments (filed Jan. 20, 2015); Shasta County, CA Sheriff Comments (filed Jan. 20, 2015); Ventura County, CA Sheriff Comments (filed Dec. 29, 2014).

²²² HRDC Comments, Exhibit A (filed Jan. 13, 2015).

²²³ HRDC Reply Comments at 2.

Marlene H. Dortch
July 21, 2015
Page 44

detecting and following-up account for 25% of the workload” for one full-time officer.²²⁴ It did not explain how the percentage was calculated or how these basic law enforcement activities should be charged to the provision of ICS.

San Bernardino County Sheriff claims the FCC proposal would reduce its IWF by 52% or \$2.45 million and asserts its annual expenditures are approximately \$456,000 per year for safety and security, \$271,700 per year for investigative and analytic tools, and \$345,600 per year for free calls mandated by statute. It did not produce any information to support its calculations such as employee salaries and hours, specific activities and tasks covered under each category, and methodology for allocating, prorating and splitting shared costs. It also overstates the ICS-related costs by including basic law enforcement activities such as investigations.

Ventura County Sheriff claims it spent \$511,538 a year or \$0.142 per minute for ICS costs and about \$2 million on IWF staff and programs. It produced certain information used to calculate its expenses including employee salaries and benefits, individual employee’s percentage of time related to ICS, and bi-weekly and annual phone support costs per employee. It broadly describes responsibilities, including several investigative tasks, but does not detail how costs might be prorated or shared and the methodology for determining the percentage. Like San Bernardino County, it overstates ICS-related costs by including basic law enforcement activities such as investigative tasks.

The nine State Department of Corrections (“DOCs”) ²²⁵ claim ICS revenues are needed to support programs unrelated to the provision of ICS, such as education programs; legal research and services; treatment programs for substance abuse and sex offenses; re-entry programs like transitional housing and bus tickets; and materials for inmates like newspapers, books, recreational and fitness equipment, furniture, and television service. If these programs and materials better serve inmates and communities, state policy makers should be willing to allocate funds for these purposes, even absent ICS commission revenue.²²⁶ Several DOCs also claim ICS revenues are needed for monitoring and investigations, but these are basic law enforcement activities and not part of the provision of ICS.

None of the DOCs attempt to quantify specific ICS costs, other than the Georgia DOC which admits that ICS costs are not clearly defined in its budget “in a way that accurately reflects its

²²⁴ Imperial County, CA Sheriff Comments at 2.

²²⁵ Arizona Department of Corrections Comments (filed Dec. 31, 2014); Georgia DOC Comments; Idaho Department of Correction Comments (filed Nov. 20, 2014); Kansas Department of Corrections Comments (filed Dec. 24, 2014); Montana Department of Corrections Comments (filed Dec. 31, 2014); Ohio Department of Rehabilitation & Correction Comments (filed Jan. 12, 2015); Oklahoma Department of Corrections Comments (filed Jan. 8, 2015); Oregon Department of Corrections Comments (filed Dec. 11, 2014); Tennessee Department of Correction Comments (filed Jan. 12, 2015).

²²⁶ See HRDC Reply Comments at 2.

Marlene H. Dortch
July 21, 2015
Page 45

overall monetary and non-monetary operational and capital expenditures associated with ICS.”²²⁷ Nonetheless, the Georgia DOC estimates its monthly costs as approximately \$167,000 by conducting a survey to identify day-to-day tasks under six categories, hours spent on each task, and salaries of employees with any involvement or interaction with ICS. This submission lacks details to validate the result because it does not describe the number of participants in survey, the identified day-to-day tasks, the method for categorizing tasks, or the method for allocating any shared costs. The Georgia DOC also did not produce a copy of the survey or any work papers.

Seven associations and groups²²⁸ submitted comments that ICS revenues are needed to support programs unrelated to the provision of ICS such as education and welfare programs. As noted above, these programs are not telecommunications services and it is not the responsibility of telecommunications consumers to pay for them.²²⁹ These commenters also assert ICS revenues are needed for crime interdiction and prosecution; monitoring; recording and providing copies of calls to law enforcement and courts; and investigative functions – all of which are basic law enforcement activities and should not be funded by ICS revenues. Furthermore, contrary to the Virginia Jail Association’s claim, maintenance and repair of equipment is handled by the provider and not the correctional facility.

A few items listed by the Oregon State Sheriff’s Association are unlikely to result in regular and/or material costs, such as writing requests for proposals and negotiating a contract, conducting background checks on provider employees with access to the facility; and training staff. Nonetheless, the Association failed to provide any documentation of such costs.

Approximately 27 form letters²³⁰ submitted by local government officials state that site commissions are necessary to their budgets and list several activities that they claim create costs. How-

²²⁷ See Georgia DOC Comments at 17-18.

²²⁸ Chief Probation Officers of California Comments (filed Jan. 5, 2015); California State Sheriffs’ Association Comments (filed Dec. 19, 2014); Florida Sheriffs’ Association Comments (filed Jan. 9, 2015); Oregon State Sheriffs’ Association Comments (filed Jan. 5, 2015); Virginia Association of Regional Jails Comments (filed Jan. 6, 2015); King George County, VA and Rappahannock Regional Jail Authority Comments (filed Dec. 22, 2014); American Jail Association Comments (filed Jan. 12, 2015).

²²⁹ See *infra*, fn. 4.

²³⁰ Graham County, AZ Sheriff (filed Dec. 3, 2015); Mohave County, AZ Sheriff (filed Dec. 22, 2014); Pinal County, AZ Sheriff (filed Dec. 15, 2014); Yell County, AR Sheriff (filed Dec. 3, 2014); Colorado Jail Association (filed Jan. 5, 2015); Columbia County, GA Detention Center (filed Dec 1, 2014); Plymouth County, IA Sheriff (filed Dec. 4, 2014); Hampden County, MA Sheriff (filed Jan. 12, 2015); Charlevoix County, MI Sheriff (filed Dec. 10, 2014); Greene County, MO Sheriff (filed Dec. 8, 2014); Gage County, NE Jail Administrator (filed Dec. 24, 2014); Cayuga County, NY Sheriff (filed Dec. 18, 2014); Niagara County, NY Sheriff (filed Dec. 8, 2014); Denton County, TX Sheriff (filed Dec. 19, 2014); Denton County, TX County Judge (filed Dec. 5, 2014); Dewitt County, TX County Judge (filed Jan. 6, 2015); Fannin County, TX County Judge (filed Jan. 7, 2015); Garza County, TX County Judge (filed Dec. 18, 2014); Hutchinson County, TX County Judge (filed Dec. 8, 2014); Panola County, TX

Marlene H. Dortch
July 21, 2015
Page 46

ever, many of those purported costs have nothing to do with the provision of ICS and are basic law enforcement activities. Such activities include surveillance, monitoring, and/or listening to calls; transporting inmates; handling US Marshal inquiries; storing calls used for court; live alert transmission costs to call investigator; prosecuting or disciplining inmates for crimes committed while using the phones; prison rape elimination act (“PREA”) mandated voicemail systems, handing calls and reporting; cell phone detection and interception systems; providing call recordings to court; free calls to public defenders, consulates, embassies and private counsel, ombudsmen; free calls to bail bond; free calls to facility commissary providers; and free booking calls.²³¹

Other items in the laundry list are associated with features and functions delivered by providers, including bandwidth costs for offering and administering platform; three-way call detection verification; and customer service. In particular, installation and maintenance of phones is handled by the provider and not the correctional facility.

A few other items are unlikely to result in regular and/or material costs, such as writing requests for proposals and handling a bidding process, litigation resulting from inmates or public about use of system, and training staff to use the system and security features. And even if any of these activities are attributable to correctional facilities for the provision of ICS, commenters did not provide any documentation of their costs.

Eight others²³² submitted comments claiming various ICS costs including: monitoring calls; investigation; maintenance of equipment; cell phone detection; educational and welfare programs; drug treatment programs; re-entry programs for housing and jobs; inmate transportation; training; installing a new ICS platform. As previously explained, many of these costs have nothing to do with the provision of ICS because they are related to basic law enforcement activities (e.g., monitoring, investigation, cell phone detection) or are beneficial to society (e.g., educational and welfare programs). Others, like installation and maintenance of phones, are handled by the provider and not the correctional facility. These commenters also did not provide

County Judge (filed Dec. 8, 2015); San Augustine County, TX County Judge (filed Dec. 2, 2014); San Patricio County, TX County Judge and Commissioners (Jan. 12, 2015); Terry County, TX County Judge (filed Dec. 8, 2014); Tuolumne County, TX Sheriff (filed Dec. 8, 2014); Waller County, TX County Judge (filed Jan. 12, 2015); Washington County, TX County Judge (filed Dec. 8, 2014); Wheeler County, TX County Sheriff’s Office (filed Dec. 3, 2014).

²³¹ See also Prison Policy Initiative Reply Comments at 7 (stating that funding of these programs “is the responsibility of government ... [not] telecommunications costs that should be paid from ICS rate revenue”).

²³² Johnson County, IA Sheriff (filed Dec. 18, 2014); Marion County, IN Sheriff (filed Dec. 29, 2014); Barnstable County, MA Sheriff (filed Dec. 24, 2014); Butler County, PA Prison Board (filed Dec. 29, 2014); Delaware County, PA (filed Jan. 20, 2015); Hemphill County, TX County Judge (Dec. 8, 2014); Taylor County, TX County Judge (filed Jan. 5, 2015); Williamson County, TX Sheriff (filed Jan. 2, 2015).

Marlene H. Dortch
July 21, 2015
Page 47

justification for the alleged costs. The Barnstable County Sheriff merely stated that a Massachusetts statute mandates the sheriff to make a return if its property and lines are used. The Taylor County Judge mentioned that its ICS contract generated \$109,000 in 2014 but did not specify how such revenues were spent. Delaware County declared that about \$1.2 million is generated from calling fees and commission to help offset expenses from inmate programs and services without providing any documentation about such spending.

3. The FCC Can Limit Site Commission Cost Payments in the Absence of Direct Evidence Regarding Correctional facilities' Costs of Providing Inmate Calling

The absence of reliable cost data for correctional facilities need not prevent the FCC from acting to place reasonable limits on site payments. The Communications Act only requires that the compensation system for ICS be “fair” to consumers and to ICS providers, not to site owners. 47 U.S.C. § 276(b)(1)(A). Moreover, if the FCC determines that permitting ICS providers to make some level of payments to site owners will promote the public interest, those payments need not necessarily be based on the site owners’ costs. The site owners, after all, are government agencies performing a public safety function, not operating a business. Correctional facilities generally do not generate net income for their operators, and have no reasonable expectation of earning revenues that will cover their costs. Nor are they managed for the purpose of returning a profit to their investors (*i.e.*, the taxpayers). It would therefore be absurd to apply a traditional “cost-plus-reasonable-return” utility regulation approach to the payment of site commissions.²³³

In any event, the FCC’s authority extends to regulating the rates and practices of ICS providers, but not the practices of correctional facilities. As explained in the undersigned’s April 8 letter, the FCC can regulate the terms on which ICS providers may contract with correctional facilities under its express and ancillary statutory authority, but this is not the same thing as directly regulating correctional facilities. The correctional facilities would remain free to decide whether they wish to enter into new contracts with ICS providers on terms consistent with the FCC’s

²³³ In *Hope Nat. Gas*, 320 U.S. at 603, the Supreme Court explained that agencies exercising rate-making authority must balance consumer and investor interests. “From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.” *Id.* (citation omitted). But there are no “other enterprises having corresponding risks” to a correctional facility, since correctional facilities are not enterprises at all, nor do they seek to attract capital in the competitive market.

Marlene H. Dortch
July 21, 2015
Page 48

requirements.²³⁴ The FCC should not (and cannot) mandate what, if any, level of services a particular correctional facility chooses to permit, nor should it compel correctional authorities to devote any portion of their facilities to ICS purposes.²³⁵ Accordingly, a regulation that solely restricts the ability of ICS providers to enter into particular types of contracts with site owners should not be vulnerable to legal challenges.

Under this approach, the FCC must consider what level of payments to facility operators would be consistent with the public interest, by creating a reasonable incentive for the facilities to continue offering ICS without imposing unjust or unreasonable costs on users of the service. GTL, based on a study performed by Economists Inc., suggests that payments in the range of \$0.005 to \$0.016 per intrastate minute of use would be sufficient to cover facilities' direct costs, although it also notes that its study did not attempt to analyze whether this would provide an incentive for facilities to lower ICS rates or ancillary fees.²³⁶ CenturyLink has suggested allowing "significant" payments without specifying a particular level, although it has also stated that the costs of call monitoring alone are at least \$0.05 per minute.²³⁷ Call monitoring, however, is a normal part of a correctional facility's internal security, like monitoring inmate mail and in-person visiting, and the cost of this function should not be recovered from telephone customers.²³⁸ A number of correctional facilities, unsurprisingly, have suggested that even larger payments are necessary to cover their costs, although as discussed in the undersigned's previous filings, few of them have provided any meaningful documentation of these supposed costs.

V. Conclusion

The FCC should not lose sight of the forest for the trees. The central issue in this proceeding is not determining the precise costs incurred by correctional facilities due to offering ICS; it is establishing reasonable rates for ICS that are fair to customers, providers, and facility operators alike. To achieve this, it should establish maximum rates for both interstate and intrastate ICS

²³⁴ As suggested in the undersigned's April 8 letter, the FCC may reasonably conclude that it should not apply any restrictions to existing contracts, at least for their current, unexpired terms; but, in that case, it would be essential to permit ICS providers to recover all the costs they incur in performing under existing contracts, including site commissions.

²³⁵ This letter does not address the merits of various sheriffs' contentions that ICS is a "discretionary" service that they have no obligation to offer to inmates; nonetheless, no such obligation is imposed by the Communications Act, and if inmates have a right to access to telephone service, it must arise under some other source of law.

²³⁶ GTL April 3 *ex parte* at 5.

²³⁷ CenturyLink Reply Comments at 20-21 & n.84.

²³⁸ Indeed, the ability to monitor ICS calls is a benefit to the facility as it improves the facility's capability to investigate potential criminal activities and other misconduct by inmates. *See* GTL April 3 *ex parte* at 5.

Marlene H. Dortch
July 21, 2015
Page 49

calls that permit providers both to recover their costs, including a reasonable rate of return on investment; and to pay a modest and reasonable, but limited, site commission to facility owners in those jurisdictions that permit such payments, to provide an incentive for continued availability of ICS in those facilities.

Sincerely,

/s/ Andrew D. Lipman

Andrew D. Lipman