

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Implementation of the Pay Telephone)	CC Docket No. 96-128
Reclassification and Compensation Provisions of the)	
Telecommunications Act of 1996)	
)	
Petition for Rulemaking, or, in the Alternative,)	DA 03-4027
Petition to Address Referral Issues in)	
Pending Rulemaking)	

***EX PARTE* WRITTEN RESPONSE OF PAY TEL COMMUNICATIONS, INC.**

Pay Tel Communications, Inc. (“Pay Tel”), by its attorneys, pursuant to 47 C.F.R. § 1.1206(b), submits this *ex parte* written response to the Reply Comments filed by the Wright Petitioners on June 20, 2007, in the above-captioned matter.

I. The Administrative Procedure Act Requires the Issuance of a Notice of Proposed Rulemaking to Consider the Merits of the Alternative Wright Petition

As shown in Pay Tel’s Comments, whatever the merits of the Wright Petitioners’ proposal, the relief sought cannot be granted in this proceeding prior to the issuance of a proper notice of proposed rulemaking. *See* Pay Tel Comments, at 3-4. Moreover, to the extent that a proper Notice is issued it must consider the full context of the inmate calling services market.

The Wright Petitioners’ proposal treats one narrow aspect of ICS, while ignoring the effects the proposal will have on the other aspects of the service. This piecemeal approach is flatly inconsistent with the Commission’s previous considerations of ICS. In its Order on Remand in this proceeding, in considering an ICS coalition’s request for relief from below-cost local collect calling rate caps, the Commission declined to require every call to make an identical contribution to shared and common costs, thereby necessitating a review of all calls—including

local and long distance—to determine whether the fair compensation requirements of Section 276 of the Communications Act had been met. *See* Order on Remand, FCC 02-39, at ¶ 23. The Commission concluded:

[T]he critical factor is that the costs must ultimately be recovered, but we will not mandate a particular method of cost recovery. Unless an ICS provider can show that (i) revenue from its interstate or intrastate calls fails to recover, for *each* of these services, both its direct costs and some contribution to common costs, or (ii) the *overall* profitability of its payphone operations is deficient because the provider fails to recover its total costs from its aggregate revenues (including both revenues from interstate and intrastate calls), then we would see no reason to conclude that the provider has not been “fairly compensated.”

Id.

Here, the Wright Petitioners seek to address only one aspect of ICS service—interstate calls from private prison facilities. It would be untenable for the Commission to deny ICS providers relief from below cost local rate caps because they had not demonstrated to the Commission’s satisfaction that overall revenues were not fully compensatory while, on the other hand, granting the Wright Petitioners’ request to drastically lower interstate long distance rates without considering whether the combination of local and long distance revenues would be fully compensatory to ICS providers. The Commission, having created this analytical structure, and having denied local rate relief to ICS providers 2002 based on this structure, cannot now abandon it to address the narrow concerns of one party.

It is also critical that any further Notice to fully consider the Wright proposal must also consider potential impact on state and federal interests. The Commission has previously noted that, “Under these circumstances, the record in this proceeding strongly suggests that any solution to the problem of high rates for inmates must embrace the states.” Order on Remand at

¶ 29. Any consideration of the issue of ICS rates must consider local and intrastate long distance rates as a component of the issue.

Finally, any Notice must consider the potential impact on legitimate penological interests. The Commission has long recognized the special nature of ICS since it is provided in penological setting where there are law enforcement, public safety, facility security, and other similar interests at stake. *See Policies and Rules Concerning Operator Service Providers*, 6 FCC Rcd. at 2752 ¶ 15 (1991) (recognizing that ICS is provided under “exceptional circumstances”). These “exceptional circumstances”—such as preventing inmates from harassing judges, jurors, victims, and potential adverse witnesses and deterring and/or preventing telecommunications—are completely ignored by the Wright Petitioners’ proposal. The issue of interstate long distance rates charges for calls from confinement facilities simply does not present itself in a vacuum. The special considerations, inherent in the nature of the service, must be considered in any further evaluation of the Petitioner’s rate proposal.

II. The Wright Petitioners’ Reply Comments and *Ex Parte* Filings Contain Numerous Misstatements and Misunderstandings

There are so many misstatements and misunderstandings in the Wright Petitioners’ Reply Comments and *ex parte* submissions that it is evident that they do not understand the ICS industry. The most serious of these misstatements and misunderstandings include the following:

1. *The Wright Petitioners’ Use of Old, Rejected Cost Data.* The Wright Petitioners have relied throughout on 1999 cost data submitted by ICS providers to the Commission in 2000. That data is not only old, it was specifically *rejected* by the Commission in the *ICS Order*, as

Pay Tel explained in its Comments.¹ Pay Tel also explained that the ICS provider coalition submitted a new cost study, in direct response to the *ICS Order & NPRM*, in May 2002, based on 2001 information.² Using FCC guidelines for a marginal facility, that study demonstrated that the average per minute cost for a local call, before post-9/11 security enhancements, was \$0.329 per minute.

Of course, that amount is sufficiently *higher than* the Wright Petitioners' proposed benchmarks that they reject it out of hand. Instead, they complain that they were "forced to use such outdated [1999] information" because ICS providers have failed to submit more recent data.³ Obviously, that statement is false, since Pay Tel pointed to the more recent cost study submitted in 2002 at the Commission's request. In addition, it assumes, incorrectly, that ICS providers are under some sort of obligation to commission a new cost study, at their own expense, in response to a Public Notice seeking comment on the Alternative Wright Petition. Naturally, the Wright Petitioners provide no citation for any authority requiring third parties to file cost studies in response to a *petition* for rule making—because there is none.⁴

In addition, the Wright Petitioners must acknowledge that any cost study must examine marginal rates, as required by the FCC. However, the Wright Petitioners reject the 2002 cost

¹ See Pay Tel Comments at 9 (discussing *ICS Order & NPRM* at ¶¶ 37-38).

² See Comments of the Inmate Calling Service Providers Coalition, CC Docket No. 96-128 (filed May 24, 2002).

³ Wright Petitioners' Reply Comments at 6.

⁴ The Wright Petitioners obviously recognize this fact since their Alternative Petition concludes with a request that the Commission order ICS providers to "submit data proving their service costs" if the Commission otherwise determines that the record is insufficient. Alternative Wright Petition at 29-30.

study on the ground that it is “irrelevant” precisely because it is derived from marginal facilities.⁵ The Commission rejected the 2000 study, among other reasons, not because the average number of calls used in the study was derived from a “marginal payphone,” but because the study did not separate the revenue and cost for local collect calls from other services.⁶

In the Commission’s *Third Report and Order* in its Payphone Proceeding, the Commission reaffirmed the use of a marginal location analysis.⁷ The Commission elected to use a marginal location analysis for two principal reasons. First, basing per-call costs and compensation levels on the number of calls at a marginal location would give payphone providers an opportunity to recover their costs, including a normal return on the assets used.⁸ Second, while the use of a marginal location does not ensure that all payphone locations will be profitable,⁹ it is consistent with Congress’s stated objective of ensuring widespread deployment of payphones. As the Commission stated: “[I]f we were to base the default compensation

⁵ Wright Petitioners’ Reply Comments, Dawson Reply Declaration at ¶ 30; *see also id.* at ¶ 16 (“There is no reason why benchmark rates should be set based upon the costs at the smallest marginal facilities”); Wright Petitioners’ Reply Comments at 18.

⁶ *See ICS Order & NPRM* at ¶ 37.

⁷ *See Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Third Report and Order, and Order of Reconsideration of the Second Report and Order, 14 FCC Rcd 2545 (1999) (“*Third Report and Order*”), at ¶¶ 139-53.

⁸ *See id.* at ¶ 139.

⁹ Specifically, the Commission concluded that “our approach is not designed to make every payphone profitable. Payphones with sufficiently low call volumes or sufficiently high costs will not be profitable, regardless of the compensation amount we establish.” *Id.* at ¶ 79. Conversely, payphones with higher call volumes may prove to be more profitable: “[W]here different locations have different levels of demand, some payphones will be more profitable than others. Moreover, no level of regulation (except possibly confiscatory taxation) could eliminate these profits. Thus, the existence of some payphones that earn positive profits does not mean that the market necessarily should be regulated.” *Id.* at ¶ 38.

amount on the average payphone location, many payphones would become unprofitable and exit the industry. We therefore conclude that we should use the marginal payphone location when establishing the default compensation amount.”¹⁰ The Commission determined that a limited number of payphone locations would be unprofitable if per-call compensation is based on a marginal location analysis, but it nevertheless concluded that a calculation of per-call costs based on the volume of calls at a marginal location “should promote the continued existence of the vast majority of payphones.”¹¹

While the Wright Petitioners would simply like to ignore the costs of providing service in jail facilities, that is Pay Tel’s business. The Wright Petitioners’ continued willful blindness to the vast majority of the calls made from confinement facilities is a form of self-absorption that cannot form the basis for policy governing the entire ICS industry.

2. *The Misplaced Focus on “Large Prison Systems.”* As Pay Tel pointed out in its comments, the Alternative Wright Petition is narrowly focused on only a small fraction of ICS. Indeed, their focus is so narrow that it is doubtful it even warrants Commission attention.¹² In just five pages, the Wright Petitioners tell the Commission no less than 15 times that they are concerned with interstate rates in “large prison facilities,” and their consultant Dawson repeats the mantra 12 times in just a few paragraphs.¹³ But the focus on “large” prison facilities not only

¹⁰ *Id.* at ¶ 141.

¹¹ *Id.* at ¶ 59.

¹² *See* Pay Tel Comments at 5-6.

¹³ *See* Wright Petitioners’ Reply Comments at 8-12; Dawson Reply Declaration at ¶¶ 8-14.

ignores the thousands of jails, the overwhelming majority of which are small or medium size,¹⁴ it ignores 60% of all prison facilities. Of the 1688 federal, state, and private prisons that existed in 2000, 1006 of them housed fewer than 750 inmates whereas 682 housed 750 or more inmates.¹⁵ And since the vast majority of calls (approaching 90%) even in prisons—regardless of size—are not interstate calls,¹⁶ it remains painfully obvious that the Wright Petitioners are concerned about only a small subset of calls from only a fraction of confinement facilities. The tail of these advocates should not be allowed to wag the dog of overarching federal policy.

3. *Improper Assumptions Concerning Facility Size.* The Wright Petitioners and their consultant seem to think that the provision of ICS services in jails can more or less be ignored since there are more inmates in prisons than in jails.¹⁷ In the first place, more than one-third (34.1%) of all inmates are in jails, which is a considerable number that cannot simply be ignored. But, equally problematically, the Wright Petitioners' improper assumptions lead to several errors. First, they assume that by simply averaging costs across all facilities, the assumed fewer interstate calls made from jails will “not have a significant impact” on the overall average cost of interstate calls, so that their proposed benchmarks “would have an extremely small impact on

¹⁴ Nationwide, 79% of jails have fewer than 249 inmates. Similarly, 80% of the jails served by Pay Tel have fewer than 249 inmates.

¹⁵ See Bureau of Justice Statistics, *Census of State and Federal Correctional Facilities, 2000* (revised Oct. 15, 2003), available at <<http://www.ojp.usdoj.gov/bjs/pub/pdf/csfcf00.pdf>>. Although the Wright Petitioners do not define what they mean by “large prison facilities,” the Bureau of Justice Statistics breaks facility size down into six subsets (<100, 100-249, 250-749, 750-1499, 1500-2499, and 2500+); 750 is the median.

¹⁶ See Pay Tel Comments at 6 & Exhibit 2.

¹⁷ See Wright Petitioners' Reply Comments at 15-16; Dawson Reply Declaration at ¶ 20.

service providers in those jails.”¹⁸ Second, their benchmarks reflect the use of less expensive high-volume special access circuits, rather than more expensive local switched lines, to interconnect with the LEC’s central office, which, it is claimed, is typical of large facilities.¹⁹ Not only do these assumptions ignore the Commission’s marginal location analysis, as well as the intertwined intrastate calls, but they reflect a poor understanding of the ICS industry. ICS providers, generally, do not provide services in both prisons and jails of all sizes. Instead, ICS providers have tended to service certain niches within the overall ICS industry. Thus, some providers focus on large state-run prisons and “mega” jails, whereas others, such as Pay Tel, focus on small and medium size jails. High-volume special access circuits are either not available to or are cost-prohibitive for providers such as Pay Tel providing ICS service in small and medium size jails, especially in rural areas. And if the Wright Petitioners’ benchmarks, averaging the costs of interstate calls in prisons and jails and ignoring the costs of intrastate calls, were adopted, it would put Pay Tel out of business.²⁰

4. *A Fundamental Misunderstanding of First Minute Costs.* The Wright Petitioners assert that “the first minute of a call does not cause any greater cost than each subsequent minute.”²¹ This is fundamentally wrong. First minutes have inherently greater costs than

¹⁸ Wright Petitioners’ Reply Comments at 16 (first quotation); Dawson Reply Declaration at ¶ 20 (second quotation).

¹⁹ Dawson Reply Declaration at ¶ 42.

²⁰ As shown in Pay Tel’s comments, interstate calls generated 16.6% of Pay Tel’s revenues in February 2007 but were only 3.7% of call volume, and Pay Tel had a profit margin in 2006 of 1.3%. See Pay Tel Comments at 6, 9. It is obvious that if the Wright Petitioners’ interstate benchmarks were adopted, without a concomitant federal preemption of state local rate caps, Pay Tel could no longer survive as a going concern.

²¹ Wright Petitioners’ Reply Comments at 22; Dawson Reply Declaration at ¶ 26.

subsequent minutes. The manner in which a call is billed is the primary determinant of those costs. Thus, billing and collection are necessarily front-loaded onto the first minute because those costs must be recouped regardless of the length of the call. Similarly, the validation process must occur in order for the call to be completed, and, again, that affects first minute costs which must be recovered. This is why ICS providers must charge per-call or set-up fees. Otherwise, they would lose money on every call that is shorter than the average duration while only recovering their costs on calls that are longer than average. No ICS provider could stay in business under this scheme.

For example, if billing and collecting costs average \$1.00 per call (*see* Pay Tel Comments, at 13), these costs must be recovered over the length of the call. Calculated on a per-minute basis, obviously, the shorter the duration of the call the more cost that must be recovered per minute. If the \$1.00 is recovered on an 8.9 minute call (Pay Tel's current average for an interstate collect call), the cost per minute for billing and collection would be \$0.112. If the \$1.00 is recovered on a 5.4 minute call (Pay Tel's current average for an interstate prepaid card call), the cost per minute for billing and collection would be \$0.185, or 65% higher than for an 8.9 minute call. Contrary to the Wright Petitioners' assertions otherwise, the average length of the call has everything to do with whether an ICS provider is able to recover its costs, and Pay Tel's experience with prepaid cards shows, without any doubt, that the imposition of a low per-minute rate cap on collect calls will drive callers to shorter duration calls.

The elimination of an upfront charge for ICS calls, even for in-house prepaid collect accounts or in-house direct bill accounts, is simply unworkable in the inmate context. In the jail environment the inmate may be arrested at 2:00 AM and need to call his mom who has chosen to use a local phone provider (CLEC or wireless carrier) that refuses to bill collect calls. With

today's ICS, the provider must provide a way to: (1) immediately inform the inmate's mom on how to establish an account to receive calls—one option is to provide a First Call Free where the inmate is allowed to speak to his mom and she is informed on how to establish an account—resulting in a new costs to ICS providers; (2) allow the inmate's mom to open an account immediately—either a Direct Bill Account for credit worthy customers or a prepaid account—resulting in a new costs for 24/7/365 customer service support to open and maintain accounts. Once again, the Petitioners flat statement that “[t]here should be no minimum amount required to set up a prepaid account” (Petitioners’ Reply Comments, at 29) again underscores the Petitioners’ total lack of understanding of how ICS is provided in a jail environment.

5. *Incorrect Discounting of Increased Costs Since 9/11.* The Wright Petitioners pooh-poo Pay Tel's statement that its costs have increased since September 11, 2001. They claim that all the additional functions that Pay Tel now has to provide were required as early as 1997 in the Federal Bureau of Prison's RFP and that they “did not arise suddenly after 9/11” and “did not spring into place after 9/11.”²² Again, these claims merely underscore their ignorance of the ICS industry. While the FBOP required numerous security measures in the late 1990s at 1000+ bed federal prisons, local jails did not. In fact, local jails at that time required virtually none of these extensive security functions. But 9/11 changed everything. After the attack and its concomitant focus on increased security, even 25 bed local jails wanted *all* the security features that the very largest federal prisons had. Post 9/11, what sheriff wanted to face the voters if he or she had not taken all precautions that were available? And those security measures have been expensive to implement in small and medium size jails, which represent 80% of Pay Tel's clients

²² Wright Petitioners’ Reply Comments at 20 (first quotation); Dawson Reply Declaration at ¶ 36 (second quotation).

as well as 80% of jails nationwide. Accordingly, costs for ICS providers serving jails have increased dramatically since 9/11, and the Wright Petitioners' ignorance of the industry cannot make those increased costs go away.

6. *Attempt to Gloss Over Fraud/Arbitrage Concerns.* As pointed out by the Alliance for Telecommunications Industry Solutions ("ATIS") Telecommunications Fraud Prevention Committee ("TFPC"), the Wright Petitioners proposal raises serious concerns regarding telecommunications fraud brought on by rate arbitrage. ATIS TFPC Ex Parte Aug. 24, 2007. If adopted, the Wright Petitioners proposal would drastically reduce interstate long distance rates—at least in some private facilities—while leaving untouched intrastate long distance and local collect calling rates. This disruption to existing pricing arrangements will cause affected inmate families to seek out artificially low long distance rates by, for example, purchasing prepaid wireless or VoIP accounts with phone numbers associated to interstate jurisdictions. The use of such arrangements raises serious fraud concerns given that the called party associated with such accounts is typically not known and the ICS provider may not have billing arrangements in place with the underlying provider.

The inmate advocates attempt to diminish this concern by seeking to discredit the ATIS TFPC as advancing an "unsubstantiated economic theory". See Washington Lawyers' Committee for Civil Rights & Urban Affairs Ex Parte Oct. 10, 2007. The Washington Lawyers' Committee, in its ex parte submission, does not identify the source of its purported expertise on issues relating to inmate fraud and abuse of the ICS system, but the ATIS TFPC is the foremost industry committee in the field of telecommunications fraud with dozens of years of actual, real-world experience in dealing with fraud in the inmate setting.

Pay Tel's experience in dealing with issues of inmate fraud supports the concerns

expressed by the ATIS TFPC. Assuming an average length of call of nine minutes—which is Pay Tel’s current average length—the Wright Petitioners’ proposal would result in long distance rates which would be lower than the current local collect call rate in 31 states. Without question, faced with this rate imbalance, inmate families would seek to take advantage of artificially low long distance rates by securing interstate telephone numbers. This trend will be exacerbated if Petitioners proposal to prohibit any per-call surcharge to recover the upfront costs of collect calls is adopted. Pay Tel has already observed the substitution of short duration calls for longer duration, more expensive calls with its prepaid card calls. *See* Pay Tel Comments, at 18 note 28.²³ If inmates have the ability, via wireless or VoIP arbitrage, to substitute a \$0.25/minute rate for a more expensive, longer duration local or intrastate long distance call, there is no question that they will do so.

The problems that this arbitrage will create for ICS service and confinement facilities are numerous. With no true visibility of the called party, inmates will be free to attempt three-way calls for harassment purposes and facility providers will not be able to identify the location of a called party. Similarly, as ICS providers do not have billing arrangements with prepaid wireless or VoIP providers, such calling substitution will lead to increases in unbillable calls, customer service costs to set up accounts and bad debt resulting from fraudulent accounts with no accurate name and address.

²³ In April 2008, Pay Tel’s average length of calls for intrastate and interstate prepaid card calls from jails show that the majority of both types of calls are five minutes or less in length (intrastate: 73%; interstate: 63%), belying the Petitioners suggesting that interstate calling patterns are substantially different from local or intrastate patterns. *See* Wright Petitioners’ Reply Comments, at 22. In fact over half (54%) of intrastate calls and nearly half (43%) of interstate calls are three minutes or less. Pay Tel’s historical data shows that the inmate population when given a choice to make a shorter call for \$.45/minute, will do so over making a
(continued . . .)

7. *Erroneous Assumptions Regarding Bad Debt.* The Wright Petitioners blithely assert that “[i]f the Commission imposes the requested inmate interstate collect calling benchmark of \$0.25 per minute, call recipients will be more able to pay their monthly long distance bills, greatly reducing uncollectibles.” Petitioners Reply Comments, at 23. This assertion is wholly unsupported by any evidence in the record and defies Pay Tel’s real world experience with this problem.

Regrettably, in the provision of ICS, bad debt is a reality regardless of the rate of the call. An analysis of Pay Tel’s bad debt for 2007 shows the percentage of bad debt for local calls averaged 27.6% while the percentage of bad debt for interstate calls averaged 19.1%. The average rate for the local calls was \$1.83, while the average rate for the interstate calls was \$11.28. This experience indicates that there are other factors influencing bad debt than simply the price of the calls. In this regard, the Wright Petitioners unsupported assertion that a reduction in bad debt from lower rates will off-set the impact of shorter, more frequent collect calls (\$.25/minute) when there is no up front surcharge to cover billing costs is inaccurate.

Once again, the Wright Petitioners failure to understand the ICS industry, resulting in fundamental errors which permeate their proposal.

III. The Wright Petitioners’ Attacks on Pay Tel Are Wholly Unfounded and Inappropriate

In their Reply Comments, the attorneys for the Wright Petitioners accuse Pay Tel of unlawfully cross-subsidizing its intrastate inmate calling services (“ICS”) with “unreasonably

(. . . continued)

10-15 minute flat rated local collect call for \$1.65 - \$2.70 or the more expensive long distance calls.

excessive” interstate ICS rates in violation of Section 201(b) of the Communications Act.²⁴ This accusation is plainly false, potentially defamatory, and an abuse of the Commission’s process.

The Wright Petitioners’ attorneys support their false accusation with citation to two cases involving AT&T from the mid-1970s,²⁵ but they selectively quote from those cases, to imply that cross-subsidization is illegal *per se*, and mislead the Commission by failing to indicate the nature of those cases. In *AT&T TELPAK*, the Commission, quoting from the Private Line Rate Cases, stated:

Care must be taken to avoid excessively high rates for a carrier’s *noncompetitive* services (or for a noncompetitive classification) which tend to offset deficiencies resulting from unduly low rates for *competitive* services.²⁶

The Wright Petitioners’ attorneys truncate the quotation after the phrase “unduly low rates” and substitute the words “for other services” instead of the quotation’s “for competitive services.”²⁷ This substitution is misleading because it elides the critical distinction between noncompetitive services and competitive services. Moreover, the implication that cross-subsidization is illegal *per se* is belied by the immediately preceding sentence that states that “cross-subsidization is

²⁴ See Wright Petitioners’ Reply Comments at 1, 7-8.

²⁵ See *American Tel. & Tel. Co., Long Lines Dep’t, Revisions of Tariff FCC No. 260, Private Line Services, Series 5000 (TELPAK)*, Memorandum Opinion and Order, 61 F.C.C.2d 587 (1976) (“*AT&T TELPAK*”), recon., 64 F.C.C.2d 971 (1977), further recon., 67 F.C.C.2d 1441 (1978), *aff’d in part, rev’d in part sub nom. Aeronautical Radio, Inc. v. FCC*, 642 F.2d 1221 (D.C. Cir. 1980), cert. denied 451 U.S. 920 (1981); *American Tel. & Tel. Co., Investigation into the Lawfulness of Tariff FCC No. 267, Offering a Dataphone Digital Service Between Five Cities*, Final Decision and Order, 62 F.C.C.2d 774 (“*AT&T DDS*”), recon. denied, 64 F.C.C.2d 994 (1977), *aff’d sub nom. American Tel. & Tel. Co. v. FCC*, 602 F.2d 401 (D.C. Cir. 1979).

²⁶ *AT&T TELPAK* at ¶ 69 (quoting 38 FCC 270, 301 (1964)) (emphases added).

²⁷ See Wright Petitioners’ Reply Comments at 8.

generally not in the public interest,” as well as by the following paragraph that “acknowledge[s] that definitiveness and certainty are presently lacking in any definition of cross-subsidy.”²⁸

Similarly, in *AT&T DDS*, the Commission stated:

Where the rates of one carrier for a service are so low as to constitute an anticompetitive practice, however, customers of that service may temporarily benefit from lower rates. This, however, is an immediate burden on ratepayers of other services, whose rates must subsidize the anticompetitive rates, and an ultimate detriment to the subsidized service’s customers, who will be deprived of the benefits of competition.²⁹

Here the Wright Petitioners’ attorneys ignore the first sentence quoted, which establishes the premise for the second sentence, then truncate the second sentence after the word “subsidize,” and substitute (again) “other services” in place of the quotation’s “the anticompetitive rates.” This selective quotation mischaracterizes the Commission’s concern with rates that are set so low as to be anticompetitive and which are only sustainable by cross-subsidization from other services not subject to competition. Indeed, the preceding and following paragraphs make it abundantly clear that the Commission was concerned with “the enormous market power and influence of AT&T” and that AT&T’s low DDS rates “would require a subsidy from monopoly services.”³⁰

In fact, it is quite troubling that the Wright Petitioners’ attorneys, fail entirely to inform the Commission that the two AT&T cases involve the danger of cross-subsidy where AT&T

²⁸ *AT&T TELPAK* at ¶¶ 69, 70 (emphasis added). In addition, it was known and established for decades, before the rise of competition to AT&T, that the “rates for interstate private line services, used solely by businesses and government, historically have been priced below their full costs while basic telephone rates have been set at or above full costs to make up the difference.” *AT&T TELPAK*, Additional Views of Chairman Richard E. Wiley at ¶ 1.

²⁹ *AT&T DDS* at ¶ 84.

³⁰ *AT&T DDS* at ¶¶ 83, 85.

could charge higher rates for *monopoly* services and use those revenues to support *below-market* rates for competitive services.³¹ Indeed, not only do they fail to inform the Commission of this context, but they go out of their way to erase that context from their selective quotations. This type of mischaracterization and misrepresentation is one thing in the course of zealous advocacy, but it is quite another when it is done to accuse an entity of illegal behavior.

Other Commission decisions from the mid-1970s demonstrate that the public interest concern of cross-subsidy focused on whether the ratepayers of monopoly services were being forced to support predatory prices for competitive services, and where a carrier did not provide monopoly services there was no such danger. Thus, in *American Satellite Corp.*, the Commission allowed a new entrant to charge rates for leased voice-grade channels that were alleged to be non-compensatory. The Commission reasoned that, “[s]ince it does not offer any basic or so-called ‘monopoly’ services whose users might be burdened as a result of losses in the competitive environment, we find no public interest justification for requiring that rates be fully compensatory at all stages of operations.”³² Similarly, in *United States Transmission Systems, Inc.*, the Commission allowed changes to the structure and rates for private line leased channel service by a small, specialized carrier that were alleged to be non-compensatory. The Commission stated that “competition” is one criterion by which the reasonableness of a rate structure may be judged under Section 201(b). After quoting from *American Satellite*, the Commission concluded that, because “USTS does not provide any monopoly type services

³¹ It was because of this danger that the Commission, in the *AT&T TELPAK* case, adopted a specific costing methodology applicable *only* to AT&T.

³² *American Satellite Corp., Revisions to Tariff FCC No. 1*, Memorandum Opinion and Order, 55 F.C.C.2d 1 (1975), at ¶ 3; *see also id.* at ¶ 5 (“It does not have mature monopoly services which it may burden with the costs of its competitive efforts.”).

which could cross-subsidize competitive offerings,” the conclusion of *American Satellite* was applicable, even though USTS was not a new entrant.³³

These two cases established the principle for what would, in just a few years, become the Commission’s policy for the treatment of non-dominant carriers.³⁴ In 1980, the Commission concluded that “marketplace forces will operate to ensure that the rates and other tariff provisions of non-dominant carriers comply with the objectives of Sections 201 and 202 of the Act” and bluntly stated that “a non-dominant competitive firm . . . will be *incapable* of violating the just and reasonable standard of 201(b).”³⁵

Of course, if the Wright Petitioners’ attorneys had reminded the Commission of any of this, it would have been immediately apparent that there is absolutely no basis for the accusation that Pay Tel has engaged in unlawful cross-subsidization in violation of Section 201(b). Pay Tel, quite obviously, is not a dominant carrier and does not provide any monopoly services. It competes with other ICS providers for contracts in jail facilities. Its interstate services are unregulated. In many instances its intrastate services are capped by state regulation at rates that are below costs. It is obvious that intrastate services charged at the maximum amount permitted by law cannot, by definition, be predatory or anticompetitive. Therefore, it is clear that the *AT&T TELPAK* and *AT&T DDS* cases have absolutely no relevance to Pay Tel’s provision of ICS.

³³ *United States Transmission Sys., Inc.*, Memorandum Opinion and Order, 66 F.C.C.2d 1091 (1977), at ¶ 5.

³⁴ *See Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, First Report and Order, 52 Rad. Reg. 2d (P & F) 215 (1980), at ¶ 36.

³⁵ *Id.* at ¶¶ 48, 88 (emphasis added).

In any event, the Commission, in the *ICS Order & NPRM*, expressly acknowledged the interrelationship between interstate and intrastate calls in the ICS context. To satisfy Section 276's mandate that payphone providers be "fairly compensated for each and every completed intrastate and interstate call,"³⁶ the Commission stated that "the critical factor is that the costs must ultimately be recovered, but we will *not* mandate a particular method of cost recovery."³⁷ Instead, the Commission held that

[u]nless an ICS provider can show that (i) revenue from its interstate or intrastate calls fails to recover, for *each* of these services, both its direct costs and some contribution to common costs, or (ii) the *overall* profitability of its payphone operations is deficient because the provider fails to recover its total costs from its aggregate revenues (including both revenues from interstate and intrastate calls), then we would see no reason to conclude that the provider has not been "fairly compensated."³⁸

By not mandating a particular method of cost recovery in allowing all costs to be ultimately recovered and in determining that all costs are recovered if *overall* profitability is not deficient as a result of the *aggregate* revenues of *both* interstate and intrastate calls, the Commission has effectively precluded any basis for the Wright Petitioners' attorneys' false accusation in this very docket.

In sum, Commission precedent, including the two AT&T cases from which the Wright Petitioners' attorneys selectively and misleadingly quote, as well as the *ICS Order* in this very docket, conclusively demonstrates that there is no legal basis for the Wright Petitioners' attorneys' accusation that Pay Tel has engaged in unlawful conduct.

³⁶ 47 U.S.C. § 276(b)(1)(A).

³⁷ *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 17 FCC Rcd 3248 (2002) ("*ICS Order & NPRM*"), at ¶ 23.

³⁸ *Id.* (emphases in original).

Conclusion

For the foregoing reasons, there is no legal basis for the Wright Petitioners' attorneys' accusation that Pay Tel has engaged in unlawful conduct and, hence, no grounds for the investigation that the Wright Petitioners call for. In addition, the plethora of misstatements and misunderstandings contained throughout the Wright Petitioners' Reply Comments actually serve to underscore the necessity that the Commission issue a new notice of proposed rulemaking in order to undertake a *complete* review of inmate calling services, one that analyzes all aspects of both local *and* long distance calls at both prisons *and* jails.

Respectfully submitted,

PAY TEL COMMUNICATIONS, INC.

/s/

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