

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

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

**COMMENTS OF
THE FREE STATE FOUNDATION***

These comments are submitted in response to the Commission's *Further Notice of Proposed Rulemaking* released May 2, 2016. The *Notice* seeks comment on the Commission's proposal to impose a new regulatory framework on so-called "special access" or "business data services" (BDS). The *Notice* proposal to regulate – or in some respects re-regulate – those services is purportedly based on the Commission's analysis of its 2015 data collection regarding BDS services.

The primary purpose of these brief comments, along with the attached appendix containing a recently published Free State Foundation *Perspectives*, is to urge the

* These comments express the views of Randolph J. May, President of the Free State Foundation and Seth L. Cooper, Senior Fellow. We acknowledge the assistance of FSF Research Associate Michael J. Horney, author of the attached appendix to these comments. The views expressed do not necessarily represent the views of others associated with the Free State Foundation. The Free State Foundation is an independent, nonpartisan free market-oriented think tank.

Commission to refrain from imposing new regulations on BDS services. New regulations would deter competitive entry and investment in next-generation IP-based broadband services to the detriment of consumers. More specifically, this comment calls attention to highly problematic aspects of imposing a building-by-building definition of the BDS market as contemplated in the Notice. Such an improper extremely narrow market definition should not be adopted.

A building-by-building definition of the DBS market would produce a distorted picture of the market that ignores the existing and potential competition. And the imposition of new rate regulation based on such a distorted picture would needlessly and harmfully deter competitive entry and investment in the DBS market. Moreover, it would constitute rate regulation of broadband services.

Today's dynamic communications market offers consumers – including business customers – an increasing variety of choices. Competitive entry into the BDS market by cable operators and 4G LTE wireless options are among the alternatives for broadband data services. A decade ago those options scarcely or never existed. These developments and their potential for future competition confirm the soundness of the Commission's Clinton Administration-era reductions of special access regulatory burdens.

Given market advancements and ongoing competitive entry and investment, the wisest and preferred course of action is for the Commission to refrain from imposing new regulatory burdens on BDS services. Cable operators are investing significant amounts of private capital to compete in the BDS marketplace. Such investments pose far better potential for enhancing BDS competition and consumer welfare than new regulation.

Moreover, mandated rate reduction of BDS services would likely have the negative effect of deterring development of further facilities-based competition – competition that, in any event, already is progressing. If the Commission forces down incumbents' rates, cable operators and other BDS competitors will have greater incentive to rely on non-facilities-based rate-regulated options. And those competitors will have correspondingly reduced incentive make significant investments to provide commercial customers with next-generation IP-based services that are more robust and less expensive than the services offered by the incumbent providers.

Nonetheless, the Commission has spent an entire decade now in a quixotic quest to determine whether – in its own data-distorted and pre-conceived notion opinion – BDS services are priced reasonably and whether to re-regulate rates for those services. Above all, it would be serious mistake for the Commission to define the BDS market on a building-by-building basis. Excessively narrow definitions of markets result in distorted pictures of competitive conditions. An extremely narrow building-by-building definition of the BDS market – which the Notice seeks comment on – would ignore competition that actually exist for BDS services. Indeed, a building-by-building market definition would ignore the potential competition posed by competitors serving neighboring buildings. Also critical to any competitive analysis of the BDS market is the number of consumers or business customers. The Notice's myopic focus on the number of competitors serving individual buildings fails to factor in the potential downward effects on pricing that results from bilateral monopoly situations where only one provider and one customer are present. These points are discussed further in the attached *Perspectives*

from *FSF Scholars* paper, "The FCC Cannot Proceed in the BDS Proceeding with a Flawed Analysis," by FSF Research Fellow Michael Horney, published on June 6, 2016.¹

The Commission, therefore, should reject calls for imposing building-by-building market definitions of BDS services and regulating them on that basis. Some geographic locations or even buildings will undoubtedly have more competitive options than others. But it is not the Commission's job to supervise the competitive conditions governing every building location and commercial contract regarding BDS services in the nation. Rather, the Commission should focus on the unmistakable, long-term trend towards more competition and more choices for consumers in most locations – a trend enabled and furthered by the deployment of lower-cost, more efficient digital technologies.

Consistent with these comments the Commission must not define the BDS market on a building-by-building basis. Instead, in a long-overdue move, it should close this proceeding. It should seek ways to facilitate continued competitive entry and investment in new facilities, rather than imposing new rate regulations based on improperly narrow market definitions and flawed data analysis.

Respectfully submitted,

Randolph J. May
President

Seth L. Cooper
Senior Fellow

Free State Foundation
P.O. Box 60680
Potomac, MD 20859
301-984-8253

June 28, 2016

¹ Michael J. Horney, "The FCC Cannot Proceed in the BDS Proceeding with a Flawed Analysis," *Perspectives from FSF Scholars*, Vol. 11, No. 17 (June 6 2016), available at: http://www.freestatefoundation.org/images/The_FCC_Cannot_Proceed_in_the_BDS_Proceeding_with_a_Flawed_Analysis_053116.pdf.



Perspectives from FSF Scholars
June 6, 2016
Vol. 11, No. 17

The FCC Cannot Proceed in the BDS Proceeding with a Flawed Analysis

by

Michael J. Horney *

On April 28, 2016, the FCC adopted a [Notice of Proposed Rulemaking](#) (NPRM) regarding the investigation and subsequent regulation of what it now calls Business Data Service (BDS), formerly “special access” services. In the “Competition Analysis” section of the NPRM, the FCC asks many questions about how it should define the BDS market. The NPRM cites a number of declarations that attempt to analyze the market for BDS. But, as much as anything else, these questions and declarations raise still further questions that will be difficult for the Commission to answer.

For some time, the FCC has purported to define the relevant BDS market by discrete “location,” which generally means a single office building or cell site. In other words, each building with a BDS connection is considered by the FCC to be its own market. Under this view, the BDS price at any building is not impacted by nearby consumers or nearby BDS providers. FSF scholars have [always rejected](#) this building-by-building market definition as improperly narrow.

The market definition apparently stems from CLECs that claim it is impossible for them to compete in markets that are connected only by an ILEC. But as Fred Campbell explains in an April 2016 [Forbes article](#), the “impossibility” of CLECs to connect to ILEC-only buildings comes down to a mere 88 feet.

According to data the FCC just released, CLECs’ claimed “impossibility” amounts to 88 feet (or less) for at least half of ILEC-only buildings circa 2013. The FCC data show that 50% of ILEC-only buildings are [within 88 feet of the nearest CLEC network](#) (and the average distance between CLEC networks and *all* such buildings is only 364 feet). In

other words, CLECs argue that price regulation is necessary because, for at least half of all ILEC-only buildings, it's "impossible" for CLECs to extend their fiber networks an additional 88 feet.

In the FCC's April 2016 white paper entitled "[Empirics of Business Data Services](#)," Dr. Marc Rysman explains how data was collected on "locations."

For the location data, a goal of the FCC was to assign locations to buildings, in part to determine competitive overlap within buildings. Identifying when two competitors are in the same building is a non-trivial problem with these data. Some data providers reported latitudes and longitudes, while others reported addresses, and even then, slightly different latitude and longitudes or slightly different addresses may actually be part of the same building for our purposes. In order to determine which customers were in the same building, the FCC assumed that locations less than 50 meters (approximately 164 feet) apart were the same building (unless the geocoded address reported that they were in distinct buildings). Naturally, this requires a procedure to address sequences of locations that are less than 50 meters apart each, but together are more than 50 meters apart. In practice, each customer in the data appears in only one building. We assign each building to a census block, which then implies its census tract and county.

How can the FCC assume that two BDS providers within 164 feet of each other are located in the same building, but at the same time claim that 88 feet is too distant for a CLEC to obtain its own connection? Not only is the FCC's BDS market analysis flawed in this regard, but so is its data collection on building locations. The FCC should not make assumptions about building locations based on inadequate data if it will be using that data to analyze the competitiveness of each individual "market."

Although the FCC's NPRM asks many questions concerning how it should analyze and define competition in the BDS market, based on recent experience the FCC likely will define the market at the building location level. Doing so will make the BDS market look less competitive than it actually is. Then, the agency will claim a need for new regulations. As I stated above, CLECs want the FCC to define the BDS market by building location. On behalf of Sprint, which operates as a CLEC in some areas, Stanley M. Besen and Bridger M. Mitchell filed a declaration asserting that "analyzing competitive conditions for special access service in [Metropolitan Statistical Areas] MSAs can be highly misleading because these large areas often contain smaller geographic areas across which competitive conditions are widely disparate." They also claim that "the appropriate geographic market for analyzing special access channel terminations is the building location."

Notably, however, Dr. Marc Rysman concludes, correctly in my view, in an FCC April 2016 white paper that there are problems with analyzing data at the building level:

There are some problems inherent in analyzing the data at the building level. It is possible that providers in nearby buildings exert competitive pressure even if they cannot immediately serve the building in question. A further problem is that many buildings may

contain only one customer, and thus we will observe only one provider regardless of how competitive the market to serve that customer is.

Dr. Rysman says that at the census block level “there is evidence that local competition affects BDS prices” and that “the effect of competition is larger in regions with regulatory pricing flexibility.” In his white paper, Dr. Rysman estimates how competition affects BDS prices, but he only analyzes competition among BDS providers and does not take into account competition among businesses who buy BDS. Although Dr. Rysman does acknowledge that demand impacts price and competition, the impact of demand on BDS prices is not the focus of his white paper. The FCC’s NPRM says that the Commission will assess business density and demand when analyzing each individual market. But analyses should be performed to estimate how consumer demand affects BDS prices throughout the United States. The price of BDS is a product of both supply *and* demand, and, therefore, it is very important to understand the effect of consumer demand on BDS prices.

As the number of consumers in any market increases, the price of one unit in that respective market will increase with all other things being equal. As the price increases due to more consumer demand, additional suppliers will be incentivized to enter the market. Therefore, however the FCC defines the BDS market, it must recognize the impact that the number of consumers has on other market outcomes, such as price and the number of BDS providers. If the FCC’s building-by-building definition were accurate, assuming BDS providers sell the same level of service to all consumers and with all else being equal, one consumer in one building would pay significantly less for one unit of BDS than what two or more consumers in another building would pay for one unit of BDS. Also, under the FCC’s building-by-building definition, a “market” with one BDS provider and one consumer should be considered a bilateral monopoly. Bilateral monopolies create a price lower than what would exist in a normal monopoly market because the single consumer has bargaining power. If the FCC is serious about its building-by-building definition of the BDS market, it should have addressed bilateral monopolies in the NPRM. But it did not.

Most importantly, as Dr. Rysman states in his white paper, nearby competition impacts BDS prices. Additionally, it would be wrong to think that the demand for BDS does not have an impact on BDS prices. The FCC should not impose regulations on BDS providers without fully understanding the competitiveness of the BDS market, and it cannot understand the competitiveness of the BDS market until it acknowledges and properly assesses the impact consumer demand has on BDS prices and the number of BDS providers.

In sum, before the FCC moves forward in this proceeding, it must be able to answer the following question: With all else being equal, is the price of BDS in buildings with only one consumer less than the price of BDS in buildings with multiple consumers? This will be a difficult, if not impossible, question to answer, given the flaws in the FCC’s building location data. But if the answer is no (and I think it will be), then it is clear that nearby providers impact price, and, therefore, BDS competition is effective.

* Michael J. Horney is a Research Associate of the Free State Foundation, an independent free market-oriented think tank located in Rockville, Maryland.