

REDACTED – FOR PUBLIC INSPECTION

January 15, 2021

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VIA ECFS

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
45 L Street, NE
Washington, DC 20554

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

Dear Ms. Dortch:

The Wright Petitioners herein submit a REDACTED version of reply comments in response to the Commission's *Fourth Further Notice of Proposed Rulemaking* in the above-referenced proceeding. The Wright Petitioners are also submitting a CONFIDENTIAL version of these reply comments pursuant to the *Protective Order* adopted for the above-captioned docket.¹ Encrypted electronic copies of the CONFIDENTIAL filing are being sent via email to the recipients.

Please contact me if you have any questions or require any additional information.

Sincerely,
/s/ Gregory R. Capobianco
Gregory R. Capobianco
Counsel for The Wright Petitioners

Enclosures

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Gil Strobel
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¹ *In re Rates for Interstate Inmate Calling Services*, WC Docket No. 12-375, Order, 28 FCC Rcd 16954 (WCB 2013).

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

In the Matter of)
)
Rates for Interstate Inmate Calling Services) WC Docket No. 12-375
)
)

**REPLY COMMENTS OF
THE WRIGHT PETITIONERS
BENTON INSTITUTE FOR BROADBAND & SOCIETY
PRISON POLICY INITIATIVE
PUBLIC KNOWLEDGE**

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INTRODUCTION AND SUMMARY

The Wright Petitioners,¹ along with the Benton Institute for Broadband & Society,² Prison Policy Initiative,³ and Public Knowledge⁴ (collectively, the “Public Interest Parties”), respectfully submit these reply comments in the above-captioned proceeding.⁵ The record confirms what incarcerated families and their loved ones have known for years: unconscionably high ICS rates inflict significant economic, social, and emotional harms impacting some of the most vulnerable members of society. Commenters agree that the economic and social consequences of high ICS rates are vast and profound. MediaJustice, et al., cite a report by the Ella Baker Center for Human Rights that observes that “one in three families with an incarcerated loved one goes into debt trying to maintain contact while enriching predatory correctional telecom corporations,” noting that maintaining such communications is necessary

¹ The Wright Petitioners—the late Martha Wright, Ulandis Forte, Ethel Peoples, Laurie Lamancusa, Dedra Emmons, Charles Wade, Earl Peoples, Darrell Nelson, and Jackie Lucas—brought suit in the United States District Court for the District of Columbia against Corrections Corporation of America in 2000, seeking to set aside exclusive telephone contracts among the private prisons and certain telephone companies. The matter was subsequently referred to the Federal Communications Commission in August 2001. Since 2003, these petitioners have actively petitioned the Commission for regulation of inmate calling services through The D.C. Prisoners’ Legal Services Project, Inc. at the Washington Lawyers’ Committee for Civil Rights and Urban Affairs.

² Benton, a non-profit, operating foundation, believes that communication policy—rooted in the values of access, equity, and diversity—has the power to deliver new opportunities and strengthen communities to bridge our divides. Its goal is to bring open, affordable, high-capacity and competitive broadband to all people in the U.S. to ensure a thriving democracy. These comments reflect the institutional view of the Benton Institute for Broadband & Society, and, unless obvious from the text, is not intended to reflect the views of its individual officers, directors, or advisors.

³ The Prison Policy Initiative (“PPI”) produces data-driven reports showing how mass incarceration hurts our national welfare. As part of this work, PPI has spent the last 8 years exposing the dysfunction of the prison and jail telephone market and advocating for the Federal Communications Commission to bring fairness to this market.

⁴ Public Knowledge is a public interest telecommunications and technology group that advocates before the Federal Communications Commission and other public and private forums for freedom of expression, online privacy, competition, access to all communications tools at affordable rates, equality of treatment for all, and other policies that benefit the public.

⁵ *In re Rates for Interstate Inmate Calling Services*, Report and Order on Remand and Fourth Further Notice of Proposed Rulemaking, 35 FCC Rcd 8485 (2020) (“FNPRM”).

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and critical to decreasing the trauma suffered by children who have an incarcerated parent.⁶

Prison Legal Services of Massachusetts describes how the burden of high ICS rates falls disproportionately on over-incarcerated communities of color.⁷ Worth Rises agrees that high rates affect marginalized communities, and further observes that these same groups have been disproportionately affected by the COVID-19 pandemic.⁸

As we explained in our initial comments, the Commission’s proposal represents a promising first step to provide much-needed relief.⁹ While some commenters legitimately criticize the data the Commission relies upon, others raise concerns plainly aimed at stopping or delaying changes that could affect provider profit. The Commission’s data, while not perfect, provides a sufficient basis for urgently needed reform and the Commission should reject calls to delay lowering the rates until all conceivable deficiencies can be corrected. Even given the inflated cost data, the record offers support for the Commission’s rate methodology, subject to certain modifications, as a reasonable approach to reducing rates. This is because the Commission’s proposal to lower the rate caps—including its use of mean plus one standard deviation and inclusion of a site commission allowance only for those portions of commissions that are supposedly “legitimate”—are reasonable choices and consistent with both *GTL* and Section 276 of the Act.

The Commission can—and should—act now with the data it has to provide needed relief to ICS ratepayers. In addition, the Commission should act on the need for future data collections

⁶ Comments of MediaJustice et al. at 1, WC Docket No. 12-375 (Nov. 23, 2020) (“MediaJustice Comments”).

⁷ Comments of Prisoners’ Legal Services, Bristol County for Correctional Justice, Greater Boston Legal Services CORI & Re-entry Project, The Coalition for Social Justice, and Karina Wilkinson at 1, WC Docket No. 12-375 (Nov. 23, 2020) (“Prisoners’ Legal Services of Massachusetts Comments”).

⁸ Comments of Worth Rises at 1, WC Docket No. 12-375 (Nov. 23, 2020) (“Worth Rises Comments”).

⁹ Wright Petitioners, Prison Policy Initiative and Public Knowledge at 4-9, WC Docket No. 12-375 (Nov. 23, 2020) (“Public Interest Parties Comments”).

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to remedy the deficiencies revealed in the Second Mandatory Data Collection, as well as regularly re-evaluate ICS rates based on newly collected data. The Public Interest Parties also urge the Commission to lower ancillary service charge caps and adjust them in the future based on new cost data, as well as ensure that incarcerated persons and their family members with disabilities are able to communicate with more advanced technologies. Finally, the record supports swift action, and the Commission should ensure that all of the adopted reforms are effective 30 days after publication in the Federal Register.

I. THE RECORD AND ICS COST DATA SUPPORT LOWERING INTERSTATE RATES, NOT DELAYING ACTION.

The record and ICS cost data submitted as part of the Second Mandatory Data Collection provide more than sufficient evidence supporting immediate rate reform. None of the arguments providers raise alleging flaws in the data collection require delay in lowering interstate rates in this proceeding. Indeed, the D.C. Circuit has held that even where data may be incomplete or flawed the Commission enjoys broad discretion to formulate a solution to a regulatory dilemma.¹⁰

The ICS providers' contentions that discrepancies in the data submissions render the data collection insufficient to support lowering rate caps are baseless. First, the ICS providers make much of the fact that they did not have a common basis to account for direct and indirect costs. The Public Interest Parties, too, noted that "the Commission did not specify a common methodology for providers to allocate their direct and indirect costs of providing ICS, or

¹⁰ "[W]e cannot require an agency to enter precise predictive judgments on all questions as to which neither its staff nor interested commenters have been able to supply certainty. 'Where existing methodology or research in a new area of regulation is deficient, the agency necessarily enjoys broad discretion to attempt to formulate a solution to the best of its ability on the basis of available information.'" *Am. Pub. Commc'ns Counsel v. FCC*, 215 F.3d 51, 56 (D.C. Cir. 2000) (quoting *Indus. Union Dep't, AFL-CIO v. Hodgson*, 499 F.2d 467, 474-75 n.18 (D.C. Cir. 1974) (citing *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 811 (1968))).

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allocating overhead costs.”¹¹ The differences in how direct and indirect costs are accounted for, however, do not undermine the Commission’s ability to lower the egregiously high interstate rates.¹² As the Brattle Reply Report¹³ concludes, the Commission’s methodological approach corrects for most of the variation in reported costs by using minutes of use to allocate the share of such costs.¹⁴ “Assuming ICS providers are not mischaracterizing their total costs, issues of allocating costs should not form a basis for delay in setting rates.”¹⁵

While it is true that the lack of a common methodology made it “difficult to verify the accuracy of the ICS providers’ reported costs,”¹⁶ it is notable that the two largest providers, GTL and Securus, each vociferously assert that *their* responses to the data collection represent their respective companies’ true and accurate ICS costs.¹⁷ Taking GTL and Securus at their word that the data each has submitted is complete and accurate necessitates that the Commission dismiss out of hand these companies’ arguments that the data collected is too flawed to be used for rate-setting. As the Brattle Reply Report correctly observes, because these two providers constitute such a substantial majority of the total minutes of use—over 76 percent—were the Commission to accept their representations of accuracy, there would already be a sufficient basis upon which to base new rates using just their data.¹⁸

¹¹ Public Interest Parties Comments at 4 (footnote omitted).

¹² *Id.* at 5-6.

¹³ The Brattle Group reply report is attached hereto as Appendix A (the “Brattle Reply Report”).

¹⁴ Brattle Reply Report at 3.

¹⁵ *Id.*

¹⁶ Public Interest Parties Comments at 4.

¹⁷ *See* Comments of Securus Technologies, LLC at 24, WC Docket No. 12-375 (Nov. 23, 2020) (“Securus Comments”) (“The suggestion that Securus overstated its costs is incorrect.”); Comments of Global Tel*Link Corp. at 16, WC Docket No. 12-375 (Nov. 23, 2020) (“GTL Comments”) (“GTL disputes the suggestion that its cost data submissions were inaccurate or overstated”).

¹⁸ Brattle Reply Report at 3-4.

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If the Commission were to delay lowering rates in response to the arguments about variations in internal cost records and lack of a common methodology, it would allow self-interested ICS providers to frustrate this proceeding by inconsistently reporting their cost data. This highlights the pitfalls of relying on “[f]inancially self-interested parties with a history of deceitful behavior.”¹⁹ The Commission must not cede its ability to set rates as a result of the actions by parties that have been shown to lack candor²⁰ and stand to directly benefit from reporting inflated costs.²¹ Rather, the Commission should reduce ICS rates on the record before it and use future data collections to improve the ICS costs reporting process and conduct rate evaluations.²²

**II. THE RECORD SUPPORTS THE COMMISSION’S RATE METHODOLOGY,
WITH MODIFICATIONS SUGGESTED BY THE BRATTLE GROUP, AS A
REASONABLE APPROACH.**

**A. Commenters Raise Compelling Arguments that Rates Should be Lower than
What the Commission Proposes.**

As we explained in our initial comments, the Commission’s proposed rates are still too high.²³ Other commenters agree that rates should be lower than the Commission’s proposal. For example, Worth Rises argues that the Commission’s proposed rates “are not supported by current practices in the field”²⁴ and instead proposes that the Commission adopt a per minute interstate

¹⁹ Worth Rises Comments at 2. The Public Interest Parties agree with Worth Rises that, if anything, self-reported cost data is biased towards overstating costs, but the cost data in the record and the Commission’s expert, reasoned analysis thereof nevertheless provides sufficient basis for the Commission to move forward with reductions in ICS rates and ancillary service charge caps to address a real and longstanding market failure.

²⁰ See, e.g., *In re Joint Application of Securus Investment Holdings, LLC*, Memorandum Opinion and Order, 32 FCC Rcd 9564 (2017).

²¹ See Worth Rises Comments at 2 & nn.3-6 (demonstrating how “providers have repeatedly demonstrated their willingness to submit inaccurate information to the Commission”).

²² See *infra* Sec. V.

²³ Public Interest Parties Comments at 3, 6-9.

²⁴ Worth Rises Comments at 4.

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rate cap of \$.05. This would save consumers of calls from state and federal prisons over \$45 million annually and call volume would increase by 1.5 billion minutes annually in the 35 prison systems impacted by such a rate.²⁵ Prisoners’ Legal Services of Massachusetts suggests the Commission’s proposal does not go far enough because the cap that is eventually adopted appears to operate both as a floor and a ceiling for rates, “as there is a strong tendency for the providers to offer rates that are not much lower than the caps.”²⁶ The Public Interest Parties reiterate that, even were the Commission to adjust its proposed rate caps subject to adjustments previously described,²⁷ ICS providers will still be overcompensated.

B. The Use of Mean Plus One Standard Deviation to Determine Rate Caps Is Reasonable.

Contrary to Securus’s claims, the Commission’s rate methodology—which begins by calculating the mean per minute contract cost and adds one standard deviation²⁸—is sound and reasonable. As the Brattle Reply Report observes, the ICS cost data is not normally distributed and the variation among the data “is in some sense large.”²⁹ Accordingly, using average cost as the basis for a rate cap would not be appropriate.³⁰ However, using a more common mean plus two standard deviations approach with this dataset would also not be appropriate due to the skew of the cost data, which results in “more observations of relatively small costs below the average cost and fewer observations of relatively higher costs above the average.”³¹ Given this skew, use

²⁵ *Id.* Worth Rises further states that “[w]hile jail figures are more difficult to estimate, assuming that the national jail average for interstate calls is the current rate cap of \$0.21 per minute, we estimate that the proposed rates would save consumers almost \$9 million annually and increase call volume by nearly 800 million minutes annually. If the rate cap was instead set to \$0.05, we estimate consumers would save over \$75 million annually and call volume would increase by 3.2 billion minutes annually.” *Id.* at 4-5.

²⁶ Prisoners’ Legal Services of Massachusetts Comments at 3.

²⁷ Public Interest Parties Comments at 8-9.

²⁸ *FNPRM*, 35 FCC Rcd at 8510 ¶ 71.

²⁹ Brattle Reply Report at 6.

³⁰ *Id.*

³¹ *Id.* at 7.

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of mean plus one standard deviation produces similar results to mean plus two standard deviations from a normal distribution.³²

For a normal distribution, “95% is a commonly used benchmark for what is acceptable with a random distribution of data. Using that benchmark here to establish a rate would imply that only 5% of observations would not be fully compensated.”³³ Using a mean plus one standard deviation with the ICS distribution results in 7% of observations being under-compensated, while using the Commission’s proposed rates results in only 5% of the jail contracts and 6% of the prison contracts being under-compensated.³⁴ However, when considering not only the number of observations that are under-compensated, but the *magnitude* of under-compensation in terms of total costs, only 1% of total prison costs and 3% of total jail costs are not compensated under the FCC’s proposed rates.³⁵ This demonstrates the validity of the Commission’s use of mean plus one standard deviation to base its rate setting using the cost data.

C. The 10% Reduction to GTL’s Costs Is Supported by the Record.

The Commission’s proposal to reduce GTL’s reported costs by 10% to account for GTL’s estimated market rents, and to then calculate interstate rate caps using those adjusted costs, is appropriate and reasonable. While GTL objects to this proposed adjustment³⁶ and Securus argues that “subjective” adjustments to the data cannot solve misreporting problems,³⁷ these arguments are without merit.³⁸ Including GTL’s invested capital when calculating rates would be, as the Commission said, “inconsistent with the well-established principle that the

³² *Id.* at 8.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.* at 10, tbl. 2.

³⁶ GTL Comments at 16.

³⁷ Securus Comments at 20.

³⁸ *See* Brattle Reply Report at 12-13.

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purchase prices of companies that possess market power are not a reliable or reasonable basis for ratemaking.”³⁹ As the Brattle Reply Report explains, “capital is a reasonable cost as it is related to funding operations, not the acquisition of a company.”⁴⁰ Additionally, contrary to GTL’s assertions,⁴¹ GTL operates in a concentrated market environment and, by any reasonable measure, exercises market power.⁴² This necessitates the Commission’s adjustment of GTL’s overstated goodwill related expenses.

GTL has only itself to blame for the Commission’s proposed adjustment, as GTL inappropriately allocated its invested capital as an ICS cost. No other respondent to the data collection included such costs. Adjusting GTL’s inflated reported cost data in order to use the cost data currently before the Commission to lower rates is neither discriminatory nor inconsistent with *GTL*.⁴³ To the extent other ICS providers had improperly included their capital costs, the Public Interest Parties presume that the Commission would have similarly proposed adjustments to such cost data as well.

Finally, the Public Interest Parties note that Worth Rises calls for a 25% across the board reduction in the ICS providers’ reported cost data.⁴⁴ Due to the widespread and well-documented exaggerations by the ICS providers both in the past and now in the recent data collection, the Public Interest Parties support any and all steps that the Commission can take to ensure that the cost data in the record best reflects providers’ true costs. The Commission can

³⁹ *FNPRM*, 35 FCC Rcd at 8517 ¶ 92 (internal quotation marks omitted).

⁴⁰ Brattle Reply Report at 13.

⁴¹ GTL Comments at 18.

⁴² Brattle Reply Report at 10-12.

⁴³ GTL Comments at 18 (“There is no justification to discriminate against GTL or to adjust its reported costs. Nor is such action consistent with the D.C. Circuit’s mandates.” (footnote omitted)).

⁴⁴ Worth Rises Comments at 3-4.

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have no expectation of fulfilling its statutory mandate to set just and reasonable rates when the ICS providers submit data that overstates their costs.

III. TO THE EXTENT SITE COMMISSIONS ARE ACCOUNTED FOR IN THE NEW INTERSTATE RATES, THE COMMISSION’S APPROACH IS REASONABLE, ESPECIALLY COMPARED TO ICS PROVIDERS’ PROPOSALS THAT WOULD EFFECTIVELY ALLOW FOR UNLIMITED SITE COMMISSIONS.

There are strong arguments that site commissions should not play any role in the Commission’s ICS ratemaking. For example, Worth Rises and MediaJustice et al. argue that the Commission should exclude the costs of security and surveillance, which often are among the functions supported by site commissions, from the rate analysis because they are not directly related to the provision of communications services.⁴⁵ Constant observation of incarcerated people is a core function of jail and prison facilities, not a function specific only to ICS.⁴⁶ Moreover, monitoring ICS calls adds nothing of value to the communications service for which incarcerated people and their friends and family pay. The Public Interest Parties agree with Worth Rises and MediaJustice that there is a reasonable basis for the Commission to exclude from its cost calculus any portion of a site commission payment that is not directly linked to the provision of ICS. Prisoners’ Legal Services of Massachusetts also argues that there “is no need or justification for a two cent markup on telephone rates.”⁴⁷

Accordingly, the Commission should continue to consider whether and to what extent site commission costs are attributable to ICS during future rate evaluations. With respect to the

⁴⁵ *Id.* at 8; MediaJustice Comments at 2.

⁴⁶ For example, a guard who spends time monitoring incarcerated people’s phone calls is a part of the core function. Visitors are not charged for the guard supervision required during in-person visits; likewise, there is no basis for ICS consumers speaking to their incarcerated loved ones to be charged a fee for the same function.

⁴⁷ Prisoners’ Legal Services of Massachusetts Comments at 5.

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current proposed rates, the Commission should reduce the proposed allowance from \$0.02 to \$0.01 in order to avoid double counting costs.⁴⁸

There is no basis to “pass through” site commissions, as some providers have proposed. ICS providers appear to misunderstand the purpose of the Commission’s site commission allowance. It is not designed to compensate a provider for any and all costs categorized as “site commissions.” Instead, it estimates the portion of site commissions that “legitimately” goes towards the provision of ICS services to ensure such costs are reasonably compensated. The Commission justifiably seeks to avoid compensating the *whole* of *all* site commissions to avoid rent seeking and other unjust or unreasonable conduct by ICS providers. Absent this limitation, the Commission would create perverse incentives for ICS providers to negotiate higher site commissions with prison and jail facilities, almost certainly covering costs unrelated to the cost of providing service. The proposal to allow for recovery of a portion of site commission costs therefore strikes an appropriate balance between the statutory mandates that ICS providers receive fair compensation and that ICS rates are just, reasonable and promote access to ICS by incarcerated people and their families and support networks.

IV. THE COMMISSION’S APPROACH IS CONSISTENT WITH *GTL V. FCC* AND SECTION 276 OF THE ACT.

A. The Commission Should Reject Arguments that Would Result in Its Inability to Set Interstate Rate Caps.

Securus and GTL essentially argue that *GTL* stands for the proposition that Section 276 precludes an ICS rate cap making *any* interstate call unprofitable.⁴⁹ As an initial matter, Securus

⁴⁸ See Public Interest Parties Comments at 7-8 & Appx. A at 14-15. The Public Interest Parties further note that while the court in *GTL* said the Commission could not categorically exclude commissions, it also said that on the remand the Commission could consider *the extent to which* portions of site commissions reflected the cost of ICS and thus are “legitimate.” *GTL*, 866 F.3d at 414.

⁴⁹ *GTL* Comments at 9 (“In *GTL*, the D.C. Circuit determined the Commission’s 2015 rate caps were ‘unreasonable’ given certain calls would be unprofitable and would deny ICS providers cost recovery.”);

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and GTL ignore the Commission’s broad, plenary authority to set just and reasonable interstate ICS rates.⁵⁰ Second, Securus and GTL misconstrue *GTL* and other Section 276 precedent upon which *GTL* relies. For example, GTL wrongly asserts that Section 276 precludes Commission rate caps where any ICS call would be rendered unprofitable because such a cap would “deny ICS providers cost recovery.”⁵¹ But GTL omits important context from the D.C. Circuit’s opinion: *GTL* reversed the Commission’s rate cap decision not for failure to ensure profit on each and every ICS call, but because the caps “would deny cost recovery for a substantial percentage of all inmate calls.”⁵² Here, the Commission has gone out of its way to ensure the costs of the vast majority of calls are recoverable, thereby ensuring fair compensation to providers.

Moreover, other precedent makes clear that Section 276 gives the Commission wide latitude when setting payphone rates. *GTL* puts much weight on *American Public Communications Council v. FCC*’s statement that Section 276 precludes the Commission from adopting rates that make calls with *above-average* costs unprofitable.⁵³ However, there is a significant distinction between a rate cap that would result in above-average cost calls (roughly half of calls made) being unprofitable and a cap under which only a small number of calls are unprofitable.⁵⁴

Even under the Commission methodology affirmed in *American Public Communications Council*, some payphone calls and payphones would have been unprofitable. In that case, the

see also Securus Comments at 11 (“to the extent calls with above-average costs in each tier are unprofitable the proposed caps do not fulfill the mandate of § 276 that ‘each and every’ inter- and intrastate call be fairly compensated”).

⁵⁰ 47 U.S.C. § 201.

⁵¹ *GTL* Comments at 9.

⁵² *Global Tel*Link v. FCC (GTL)*, 866 F.3d 397, 414 (D.C. Cir. 2017) (emphasis added).

⁵³ *Id.* (citing *Am. Pub. Commc’ns Council*, 215 F.3d at 54, 57-58).

⁵⁴ Brattle Reply Report at 8-9 & tbl. 1.

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Commission had used the average cost of deploying a payphone as the basis of setting the rate payphone providers could recover from long distance carriers for each dial around call from a payphone. Neither the court nor the Commission made any inquiry into how many payphones were more or less costly to deploy than the average or whether the amount set covered particular calls. It was within the Commission’s broad authority under Section 276 to determine the methodology for the rate to be paid to assure that the compensation met the statutory “fairly compensated” standard.

Moreover, the court in *American Public Communications Council* held that, under Section 276, the Commission may rely on data from providers that contains a variety of averages and from that data assign a cost sufficient to compensate the *marginal*—break even—payphone impacted by the applicable rate.⁵⁵ Despite the fact that such analysis, which relied on imprecise data, inevitably would preclude cost recovery for each and every individual call, the court upheld this approach as a reasonable and lawful exercise of Commission discretion in rate-setting under Section 276.⁵⁶

To the extent a limited number of calls have costs that exceed the rate caps, the Commission has proposed that ICS providers can seek a waiver. Where an ICS provider can demonstrate that, on such rare occasions, certain calls cannot be compensated under the Commission’s rate cap, good cause may be found for the Commission to waive the cap. It should be noted, however, that there should be no need for the Commission to routinely grant ICS rate cap waivers because the *FNPRM* already addresses outliers through its mean plus one standard deviation approach, and because the record shows that the vast majority of ICS rates

⁵⁵ *Am. Pub. Commc’ns Council*, 215 F.3d at 57-58.

⁵⁶ *Id.*

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will remain below the caps proposed in both the *FNPRM* and comments of the Public Interest Parties.

B. Arguments that the Proposed Site Commission Allowance Is Unlawful Are Without Merit.

Securus also misreads *GTL* in suggesting that it requires that “ICS providers must be compensated for the full cost of site commission[.]”⁵⁷ *GTL* holds that the Commission cannot categorically exclude site commissions where they are “a condition precedent to ICS providers offering their services.”⁵⁸ However, *GTL* does not find that all site commission costs must be treated with the assumption that they are exclusively associated with ICS, and therefore fully recoverable through ICS rates. In light of the court’s rejection of the Commission’s prior assertion that “site commissions ‘have nothing to do with the provision of ICS,’”⁵⁹ the *FNPRM* does account for site commission costs incurred by ICS providers—although we maintain it does so perhaps too generously.⁶⁰ As explained in the Brattle Reply Report, full recovery of site commissions would reward the transfer of market power,⁶¹ exacerbating the market failure rather than correcting for it. The Commission’s limitation of cost recovery for site commissions, therefore, is appropriate and lawful.

PayTel’s approach to site commission compensation is also misguided. Section 276’s fair compensation requirement applies to intrastate and interstate calls;⁶² the allocation of a portion of the rate established pursuant to either the *FNPRM* or the Public Interest Petitioners’ proposal allows for a reasonable and fair allocated portion of the cost of a site commission to be

⁵⁷ Securus Comments at 29.

⁵⁸ *GTL*, 866 F.3d at 413.

⁵⁹ *Id.* (citation omitted).

⁶⁰ Public Interest Parties Comments at 7-8.

⁶¹ Brattle Reply Report at 14; *see also* Public Interest Parties Comments at 7 n.36 (explaining that the Commission has held that commission payments are a transfer of locational monopoly power).

⁶² 47 U.S.C. § 276(b)(1).

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compensated on a per-call basis. As with other outlier costs, where a particular provider’s site commission costs are such that the applicable ICS rate does not permit cost recovery, the waiver procedure is the appropriate relief valve.

Finally, the Commission should not seriously consider NCIC Inmate Communication’s argument that not including a greater site commission allowance raises 10th Amendment concerns.⁶³ The Commission’s proposed action does not, nor could it, affect a state’s ability to require or permit site commissions, and nothing in the *FNPRM* suggests the Commission believes or intends it has such authority.⁶⁴ Instead, the *FNPRM*’s proposal is the reasonable result of the Commission’s assessment of cost data provided by ICS providers and their allocation of a portion of ICS costs to site commissions based on the difference between costs reported at facilities with and without such commissions. Such exercise of the Commission’s authority to evaluate ICS costs and establish just and reasonable rate caps can hardly infringe upon the rights reserved to the states to charge site commissions to ICS providers.

V. THE RECORD REFLECTS THE NEED FOR FUTURE DATA COLLECTIONS AND REGULAR RATE EVALUATION.

The record confirms that the Commission should develop a new and regular data collection that requires ICS providers to properly and unambiguously allocate their costs, which will enable the Commission to engage in regular rate reviews. Like the Public Interest Parties,⁶⁵ Free Press supports conducting routine future ICS cost data collections and implementing a

⁶³ Comments of NCIC Inmate Communications at 4-5, WC Docket No. 12-375 (Nov. 23, 2020) (“NCIC Comments”).

⁶⁴ Even assuming, *arguendo*, that the proposed regulations create a tension with states’ authority to demand site commissions, federal preemption requires the states to cede ground here. “[R]ecognizing that the prescribed regulations would trench on state authority, Congress provided that section 276 preempts state law ‘[t]o the extent that any State requirements are inconsistent with the Commission’s regulations.’” *New England Pub. Commc’ns Council, Inc. v. FCC*, 334 F.3d 69, 71 (D.C. Cir. 2003) (quoting 47 U.S.C. § 276(c)).

⁶⁵ Public Interest Parties Comments at 15-17.

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biennial or triennial review process to evaluate rates based on those data collections.⁶⁶ If anything, this proceeding has shown that ICS providers continue to charge unjust and unreasonable rates and impose unconscionable fees for ICS service. Because sunshine is the best disinfectant, simply by requiring annual cost data submissions from providers and adopting a regular rate evaluation process, the Commission would create disincentives for ICS providers to abuse or skirt the Commission’s rules. As an added benefit, requiring routine cost data submissions “may incentivize ICS providers to collect more uniform and consistent data over time,”⁶⁷ which would help improve the rate evaluation process as well.

In addition to the need for future data collection and rate evaluation, flaws in the Commission’s most recent data collection can be corrected in future data collections. Many commenters note the variations and distortions that resulted from a lack of standardization of reporting and common definitions, as well as the absence of clear and explicit directions on how to account for and report certain costs. Securus, for example, suggests that a future “data collection should provide more specific instructions to each company on how to measure direct and indirect costs and should require each company to provide detailed work papers.”⁶⁸ The Public Interest Parties agree.⁶⁹ The Commission can and should create a more robust and reliable future data collection to allow for better cost evaluation going forward.

Finally, GTL’s argument that the existing annual reporting and certification requirements can serve as a basis for the Commission to ensure just and reasonable rates is misguided.⁷⁰ Currently, the Commission requires ICS providers to report their rates, the amount of any

⁶⁶ Comments of Free Press at 6, WC Docket No. 12-375 (Nov. 23, 2020) (“Free Press Comments”).

⁶⁷ *Id.* at 7.

⁶⁸ Securus Comments at 15.

⁶⁹ See Public Interest Parties Comments at 16 (“Additionally, the Commission should standardize the allocation methodology for calculating indirect costs.” (internal quotation marks omitted)).

⁷⁰ GTL Comments at 36.

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ancillary service charges and the instances of use of each, the amount of each site commission paid, and a variety of service related metrics such as minutes of use, number of TTY-based calls per facility, and the number of dropped calls experienced with TTY-based calls.⁷¹ Put simply, the current requirements measure existing rates and ancillary charges. The Commission does not regularly collect *cost* data that speaks directly to future ratemakings. The record demonstrates the need for routine ICS rate evaluation, which can only be accomplished if the Commission requires future ongoing ICS cost data collections.

VI. THE COMMISSION SHOULD LOWER ANCILLARY SERVICE CHARGE CAPS AND ADJUST CAPS IN THE FUTURE BASED ON NEW COST DATA.

The record confirms that the Commission should reexamine its approach to ancillary service charges and immediately reduce ancillary service charge caps by 10%. Ancillary service charges play a key role in the unconscionable prices incarcerated people and their friends and family pay for ICS calls. The Public Interest Parties agree with NASUCA’s “concern regarding the continued growth in the number and dollar amount of ancillary service charges and the fact that such charges inflate the effective price of ICS.”⁷² NASUCA correctly points out that ICS providers (1) often charge both an automated payment fee and a credit or debit card fee,⁷³ and (2) appear, in some cases, to share the money transfer fees charged by third parties such as Western Union and MoneyGram.⁷⁴ NCIC agrees, as it “urges the FCC to modify its rules relating to third-party transaction fees that are passed on to inmates and their families in connection with

⁷¹ 47 C.F.R. § 64.6060.

⁷² Comments of National Association of State Utility Consumer Advocates at 2, WC Docket No. 12-375 (Nov. 23, 2020) (“NASUCA Comments”).

⁷³ *Id.* at 3.

⁷⁴ *Id.*

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single calls.”⁷⁵ NCIC rightly highlights the pending federal lawsuit filed against Securus and GTL concerning single call transaction fees.⁷⁶

These and other rent-seeking abusive practices by ICS providers needlessly drive up the price of ICS calling. Like NASUCA, the Public Interest Parties urge the Commission to clarify that “payment card fees are included in, and may not be added to, the \$3.00 automated payment fee”⁷⁷ and that ICS providers may not share in the fees for services they do not provide.⁷⁸ More broadly, the Commission must enforce its ancillary service charge rules, including by initiating enforcement proceedings against ICS providers that are currently violating the rules. In addition, the Public Interest Parties reiterate that an immediate 10% reduction to all ancillary service charge caps would be appropriate pending new cost data in a future collection.

The Commission must not delay taking action on ancillary service charge caps and should act quickly to address ancillary service charge abuse by, among other things, cutting the existing ancillary service charge caps by 10%. As noted above, the record demonstrates ongoing abuses by a number of ICS providers, and those abuses directly harm incarcerated people and their support networks across the country. The *FNPRM* explicitly sought comment on whether the Commission’s “ancillary services fee caps should be lowered or otherwise modified.”⁷⁹ Therefore, GTL’s suggestion that the Commission issue a separate notice regarding changes to ancillary service charge caps is without merit. Indeed, that GTL and other commenters addressed reductions to the Commission’s ancillary service charge caps demonstrates that the *FNPRM* provided sufficient notice that the Commission could take such action. Of course,

⁷⁵ NCIC Comments at 2.

⁷⁶ *Id.* at 3.

⁷⁷ NASUCA Comments at 3.

⁷⁸ *Id.*

⁷⁹ *FNPRM*, 35 FCC Rcd at 8532 ¶ 131.

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taking action to reduce abusive ancillary service charge caps does not preclude the Commission from taking additional action to further reduce the caps based on future cost data it receives.

Finally, the Commission’s existing complaint process offers an insufficient solution and does not provide the necessary relief to incarcerated persons.

VII. THE COMMISSION SHOULD ENSURE THAT INCARCERATED PERSONS AND FAMILY MEMBERS WITH DISABILITIES ARE ABLE TO COMMUNICATE IN A FUNCTIONALLY EQUIVALENT MANNER.

The Public Interest Parties agree with the Accessibility Coalition, Free Press, and MediaJustice, who argue that the Commission has an obligation to ensure incarcerated persons have access to functionally equivalent communication services.⁸⁰ As the Accessibility Coalition explained, the current framework effectively traps incarcerated individuals with communications disabilities in a “prison within a prison.”⁸¹ The Public Interest Parties agree that the Commission should “act immediately on behalf of imprisoned people who are deaf or experience other communications disabilities.”⁸²

ICS providers should be required to offer more up-to-date Telecommunications Relay Services (“TRS”), since TRS technologies have greatly improved in recent years, and teletypewriter (“TTY”) access is no longer sufficient. Not only are TTY services technologically obsolete as a result of the transition away from analog communications systems, but also TTY-based relay services are inadequate for many people since they presume that users will be literate in English. The Public Interest Parties agree with the Accessibility Coalition that newer forms of

⁸⁰ See Comments of Helping Educate to Advance the Rights of Deaf Communities - HEARD et al., WC Docket No. 12-375 (Nov. 23, 2020) (“Accessibility Coalition Comments”); Free Press Comments; MediaJustice Comments; *see also* Comments of Sorenson Communications, LLC and CaptionCall, LLC, WC Docket No. 12-375 (Nov. 23, 2020) (“Sorenson Comments”).

⁸¹ See Accessibility Coalition Comments at 2.

⁸² MediaJustice Comments at 2; *see also* Sorenson Comments at 3 (arguing that “communications tools available to incarcerated Deaf and hard-of-hearing person[s] must” improve).

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TRS, such as video relay service (“VRS”), Internet Protocol Captioned Telephone Service (“IP CTS”), Real-Time Text (“RTT”), and other services better comply with the ADA’s functional equivalence mandate.⁸³

The Public Interest Parties also agree with the Accessibility Coalition that the Commission, pursuant to its authority under Section 225(a) and Title IV of the ADA, must require ICS providers to offer better relay and accessible communications services, and also that the Commission is obligated to take an active role in seeing that those updated requirements are followed. Accordingly, the Commission should reject GTL’s assertion that Commission action to promote disability access “must be consistent with correctional facility policies and preferences.”⁸⁴ The Commission should not unnecessarily limit itself when fulfilling its statutory obligation to ensure access. Indeed, doing so would tacitly approve of the unjust treatment of incarcerated persons with communications disabilities.

VIII. THE RECORD SUPPORTS AN EFFECTIVE DATE FOR NEW RATES SOON AFTER ADOPTION.

Given that incarcerated persons, their families, and their loved ones have suffered for years with unreasonably high ICS rates, any new rates that the Commission adopts should take effect as soon as possible. The Commission should not adopt a staggered implementation process⁸⁵ or delay the effect of new rates beyond 90 days as suggested by the California State Sheriffs’ Association.⁸⁶ The Public Interest Parties agree with Free Press that a 30-day effective period is more than sufficient.⁸⁷ As Free Press notes, even in the absence of a regulatory

⁸³ See Accessibility Coalition Comments at 7-16.

⁸⁴ GTL Comments at 37.

⁸⁵ *Id.* at 12-14.

⁸⁶ Comments of the California State Sheriffs’ Association at 2, WC Docket No. 12-375 (Nov. 23, 2020).

⁸⁷ Free Press Comments at 5.

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mandate, ICS providers have implemented rate changes in far less than 90 days in the past.⁸⁸

Therefore, the fact that ICS providers have met previous 90-day transition periods should not establish that as a default transition period. Instead, 90 days should “represent the outermost bounds of the transition time required.”⁸⁹ Where possible, as it is here, the Commission should make new ICS rates effective 30 days after publication in the Federal Register.

CONCLUSION

The Public Interest Parties urge the Commission to move swiftly to reduce interstate rate and ancillary service charge caps and provide much needed and long-overdue relief to incarcerated people and their families.

Respectfully submitted,

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⁸⁸ *Id.*

⁸⁹ *Id.* at 6.

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January 15, 2021

REDACTED – FOR PUBLIC INSPECTION

Appendix A

“REDACTED – FOR PUBLIC INSPECTION”

Brattle Report

REPLY COMMENTS ON “RATES FOR INTERSTATE INMATE CALLING SERVICES” THE FEDERAL COMMUNICATIONS COMMISSION’S REPORT AND ORDER ON REMAND AND FOURTH FURTHER NOTICE OF PROPOSED RULEMAKING (WC DOCKET NO. 12-375)

PREPARED BY

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January 15, 2021

JANUARY



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Executive Summary

The following reply report addresses some of the claims made by the ICS providers and proposes future adjustments to the Federal Communications Commission's (FCC) data collection process. In this report, we address several issues related to the data collection and various aspects of the rates proposed by the FCC. First, we discuss the criticisms levelled against the FCC's data collection and show that both the data and the underlying FCC analyses are appropriate for setting the rates. Specifically, we show that by their own admission, the current data that the Commission bases its rates on are the best available, and should not form the basis for objecting to the accuracy of the data or challenging the Commission's calculated rates. Additionally, we support the Commission's finding that facility size has no significant impact on the rates. Second, we show that the mean plus one standard deviation metric for setting the rates is appropriate given the nature of the ICS cost distribution. We provide detailed analysis of the ICS cost distribution, and show that given the variance and skewness of the distribution, the mean plus one standard deviation metric provides a similar magnitude of under-compensation as would be produced by using a mean plus two standard deviation metric in the case of a symmetric normal distribution. Third, in this report, we also examine GTL's assertion that the FCC's cost adjustment is incorrect and refute the company's claim of no market power, and provide support for the FCC adjustment. Fourth, we also address the misunderstanding of the site commission allowance, and explain that the intent of the allowance was not to compensate for site commissions, but to compensate for the portion of the commission that may have been used to provide services related to ICS. Fifth, and lastly, we propose a simplification of the data collection for future proceedings.

I. Introduction

The Brattle Group submitted an initial report in this matter on November 23, 2020 (“First Report”).¹ In the First Report, we reviewed the Commission’s approach to calculating new ICS rate caps for interstate calls. We also addressed two inconsistencies in the methodology, and commented on the general framework and certain distortions and assumptions in the analysis.

A number of ICS providers submitted comments and economic reports in the same matter.² The issues raised in these reports do not merit delay in lowering the current rates to the FCC’s proposed rates. Some providers, such as Global Tel*Link Corporation (“GTL”) and Securus Technologies, LLC. (“Securus”), argue that the FCC’s data collection suffers from various problems, and therefore should not be used to establish rates. These providers also argue that the mean plus one standard deviation metric used by the FCC to establish the rates is not appropriate. Additionally, GTL also argues that the cost adjustment made by the Commission to its data is incorrect. Providers also misconstrue the site commission allowance and argue that the allowance does not cover the site commission costs. In this report, we discuss why the issues raised have no merit.

This report comprises five sections in addition to the introduction and conclusion. In Section II, we discuss the criticisms levelled against the FCC’s data collection and show that both the data and the underlying FCC analyses are appropriate for setting the rates. In Section III, we show that the mean plus one standard deviation metric for setting the rates is appropriate given the nature of the ICS cost distribution. In Section IV, we examine GTL’s assertion that the FCC’s cost adjustment is incorrect and refute the company’s claim of no market power, and provide support for the FCC adjustment. In Section V, we address the misunderstanding of the site commission allowance. In Section VI, we propose a simplification of the data collection for future proceedings. Section VII concludes.

¹ All terms defined in the First Report remain so defined in this reply report.

² We have reviewed the Confidential Expert Report of Don J. Wood on Behalf of Pay Tel Communications, Inc., dated November 23, 2020 (“Pay Tel Economic Report”), Report in Support of Comments of Global Tel*Link Corporation submitted by Paul E. Godek, dated November 23, 2020, (“GTL Economic Report”), and FTI Consulting, Inc. Inmate Calling Services Cost Analysis for Securus Technologies, LLC., dated November 2020 (“Securus Economic Report”) as well as the accompanying legal comments (referenced below as “GTL Comments” and “Securus Comments”).

II. The Data Collection Issues that the ICS Providers Point to have Little Bearing on the FCC Methodology and Rates

A. The Data Collected Are Adequate to Calculate Per-minute Rates for ICS

The ICS providers, as well as their economic experts, claim that the Second Mandatory Data Collection was inadequate. Therefore, they argue, the results of any analysis based on these data must be dismissed.³ GTL goes so far as to compare the FCC’s data collection process to “attempting to describe the variation of climates across different regions, while ignoring the fact that some regions report temperatures in Fahrenheit and others in centigrade; that some regions report rainfall in inches and others in centimeters.”⁴ This analogy is flawed and greatly exaggerated. The data collection process undertaken by the FCC, and completed by the ICS providers, is complicated by nature. However, the unit of measurement that forms the basis of the proposed rates is the same across all ICS providers: the dollar value cost of providing ICS services.

Variation in internal cost records and reporting drives the variation in how costs are reported. That variation is largely in the reporting of direct and indirect costs – not the overall level of costs. The FCC sets the rate caps based on contract-level costs.⁵ The FCC’s allocation methodology – to use minutes of use to allocate shares of costs – is reasonable and, importantly, is applied consistently across all providers. This corrects for most of the variation in how the costs are reported. ICS providers argue for redoing the reported costs, and using detailed cost studies, but do not establish that doing so would have a meaningful impact on final rates. Assuming ICS providers are not mischaracterizing their total costs, issues of allocating costs should not form a basis for delay in setting rates.

Furthermore, due to market concentration, Securus and GTL alone account for 76% of the total paid MOU in the ICS data.⁶ Therefore, the reporting by these two providers disproportionately impacts the cost basis. In other words, the accuracy of reporting by Securus and GTL disproportionately impacts the accuracy of

³ See, for example, GTL Economic Report, ¶ 29, Securus Comments, pp. 16-17, and Pay Tel Economic Report, pp. 7-9.

⁴ GTL Economic Report, ¶ 29.

⁵ FCC, “FCC ICS 2020 FNPRM,” ¶ 76.

⁶ See Table 3 breakdown of total paid MOU by ICS provider.

the overall data. Both Securus and GTL claim that their cost data is “accurate,” and “truthful,” which necessarily applies to the vast majority of reported minutes.⁷ According to GTL:

“The ICS provider cost data submitted in response to the Second Mandatory Data Collection represents “the best underlying data available that can be verified by interested parties and the Commission” with “[a]ll data, formulas, and other aspects of the models” being “made available to other parties for their evaluation.” “The Administrative Procedure Act “does not ‘demand the perfect at the expense of the achievable.””⁸

Therefore, by their own admission, the current data that the Commission bases its rates on are the best available and do not form a basis for objecting to the accuracy of the data or challenging the Commission’s calculated rates.

B. The FCC Analysis Supporting the Rate Calculation is Sound

The ICS providers also raise issues with the FCC’s analysis based on the data collected, specifically that facility size does not have a significant impact on costs.⁹ As we mention above, the ICS providers claim that the Second Mandatory Data Collection was inadequate, and therefore, the FCC’s conclusions are incorrect. For example, GTL claims, “[g]iven the lack of a consistent reporting methodology, all of the 2020 FNPRM’s empirical analyses of costs — contained in Appendices E, F, and H — are invalid.”¹⁰ But the ICS providers’ evidence of the analysis being incorrect consists entirely of disagreement with the conclusions. Specifically, Securus claims that, “[d]ue in part to the... inconsistencies in the raw data, the results are *incompatible with the common experience of ICS providers*”¹¹ and that the conclusions are “counter-intuitive and runs contrary to the expectations on which the Commission based its ratemaking decision in 2015.”¹² Securus is claiming that the FCC’s findings cannot be correct because they do not comport with Securus’ expectations (for example, about the impact of facility size on costs).

⁷ Securus notes that its reporting is accurate and truthful, Securus Comments, p. 24. GTL also “disputes the suggestion that its cost data submissions were inaccurate or overstated,” GTL Comments, p. 16.

⁸ GTL Comments, p. 16.

⁹ Securus Comments, p. 17; GTL Pay Tel Economic Report, pp. 3, 25.

¹⁰ GTL Economic Report, ¶ 29.

¹¹ Securus Comments, p. 16. Emphasis added.

¹² Securus Comments, p. 17.

The FCC’s analyses and rate basis are not derived from expectations. Instead, the FCC uses an econometric technique called the Lasso (least absolute shrinkage and selection operator) to understand the factors that have significant explanatory power in explaining rates.¹³ This technique is an improvement on the standard Ordinary Least Squares methodology and increases prediction accuracy and the ease of interpretation. The FCC uses this methodology as an additional check, to see if there are factors that influence the per-minute costs and whether the rate setting should take these into account. The FCC states that if there are factors that are significantly related to per-minute costs, “it might be appropriate to set rates that vary according to the variables we identified.”¹⁴ They find that 71% of the variation in the per-minute costs can be explained by the provider identity and the state where the facility is located. They also find that the costs for jails are 18% greater than that of prisons and do make an adjustment for jails in their proposed rates.¹⁵

That size does not impact costs is not an unreasonable expectation. The data reflect that a large part of the expenses are overhead and fixed costs that have a weak connection to facility size.¹⁶ Even if size did have some impact on costs, that impact would have to be shown to be significant enough to have an impact on the final rates to cause carriers to be undercompensated before this concern would have merit.

III. The Mean plus One Standard Deviation is an Appropriate Basis for Establishing a Rate Given the Context and Data

Securus claims that the FCC does not provide an explanation for why it uses the mean plus one standard deviation as the basis for its rate setting.¹⁷ In the FNPRM, the FCC explains that using the industry-wide average cost in rate setting is “not novel” and has been affirmed by the Supreme Court “on more than one occasion.”¹⁸ Further, the FCC proposes adding one standard deviation, which accounts for variation from the mean in the cost data.¹⁹

¹³ Robert, Tibshirani, “Regression Shrinkage and Selection Via Lasso,” *Journal of the Royal Statistical Society, Series B (Methodological)*, Vol. 58(1), 1996, pp. 267-288, <http://statweb.stanford.edu/~tibs/lasso/lasso.pdf>.

¹⁴ FCC, “FCC ICS 2020 FNPRM,” Appendix F, ¶ 1.

¹⁵ FCC, “FCC ICS 2020 FNPRM,” Appendix F ¶¶ 4, 7.

¹⁶ For example, indirect costs as a percentage of total costs range from as low at 10% to as high as 76%. Calculated from the confidential one-time filings as part of the Second Mandatory Data Collection.

¹⁷ Securus Comments, p. 19.

¹⁸ FCC, “FCC ICS 2020 FNPRM,” footnote 212.

¹⁹ The FCC does not explicitly say this, but suggests it is correcting for variation when talking about jails that they show a “greater variations from mean costs for jails than prisons (and therefore a greater standard deviation from the mean for jails than prisons).” FCC, “FCC ICS 2020 FNPRM,” ¶ 74.

A. Using Average Costs as a Metric

Rate setting is often based on average cost (without accounting for the standard deviation).²⁰ When setting a rate based on costs, there is always some variation in costs. In most settings where average cost is used to set a rate, there is an understanding (perhaps implicit) that the variation in the cost data is sufficiently small such that any potential under-compensation (for providers with costs above average costs) is acceptable.²¹ By design, on average, any under-compensation is balanced against over-compensation. Typically, the distribution of costs is also normally distributed, implying that the distribution of under- and over- compensation is also balanced. However, in cost distributions with large variances, arguments have been made against using the average cost as a rate-setting metric.²² The FCC's addition of one standard deviation to the mean is in effect a way to make sure the portion of the distribution of providers that are potentially under-compensated falls within this acceptable range seen when variances are not large.

Using the average cost as the basis for a rate cap is appropriate in most cases because it accounts for the distribution of costs, while limiting the magnitude of over-compensation. However, in the case of the data provided by the ICS providers, using the mean as the rate basis would not be appropriate because the variation in costs is in some sense large.²³ The problem is further exaggerated because the data are not normally distributed. Instead, the cost data reported by the ICS providers has a large variance and is right-skewed.²⁴ Compared to a normal distribution with a skewness of zero, the ICS cost distribution has a skewness of 7.5, i.e. it is positively skewed. These data are skewed to the right and the right tail is longer

²⁰ In economics, this is referred to as “average cost price setting.” Examples of using the average cost to set rates include the Internet Protocol Captioned Telephone Service proceeding, regulation of Ontario energy prices by the Ontario Energy Board, and regulation of natural gas pipeline prices by the Federal Energy Regulatory Commission . See FCC’s “Misuse of Internet Protocol (IP) Captioned Telephone Service; Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities,” CG Docket Nos. 13-24, 03-123, August 30, 2017; Ontario Energy Board, “Regulated Price Plan Price Report,” November 1, 2020-October 31, 2021; Federal Energy Regulatory Commission, “Cost-of-Service Rates Manual,” June 1999, <https://www.ferc.gov/industries-data/natural-gas/overview/general-information/cost-service-rate-filings>.

²¹ In addition to concerns about inflated cost data, reported costs typically have an accounting for uncertainty and other buffers that suggest that even if “reported” costs are not fully covered “actual” costs might be. For any provider whose actual costs are not compensated, in the FNPRM, the Commission has proposed a waiver process for outliers. ICS providers can “seek waivers on a facility-by-facility or contract basis” if the proposed rate caps “prevent the provider from recovering the costs of providing interstate inmate calling services at that facility or at the facilities covered by that contract.” See FNPRM ¶¶ 108-111.

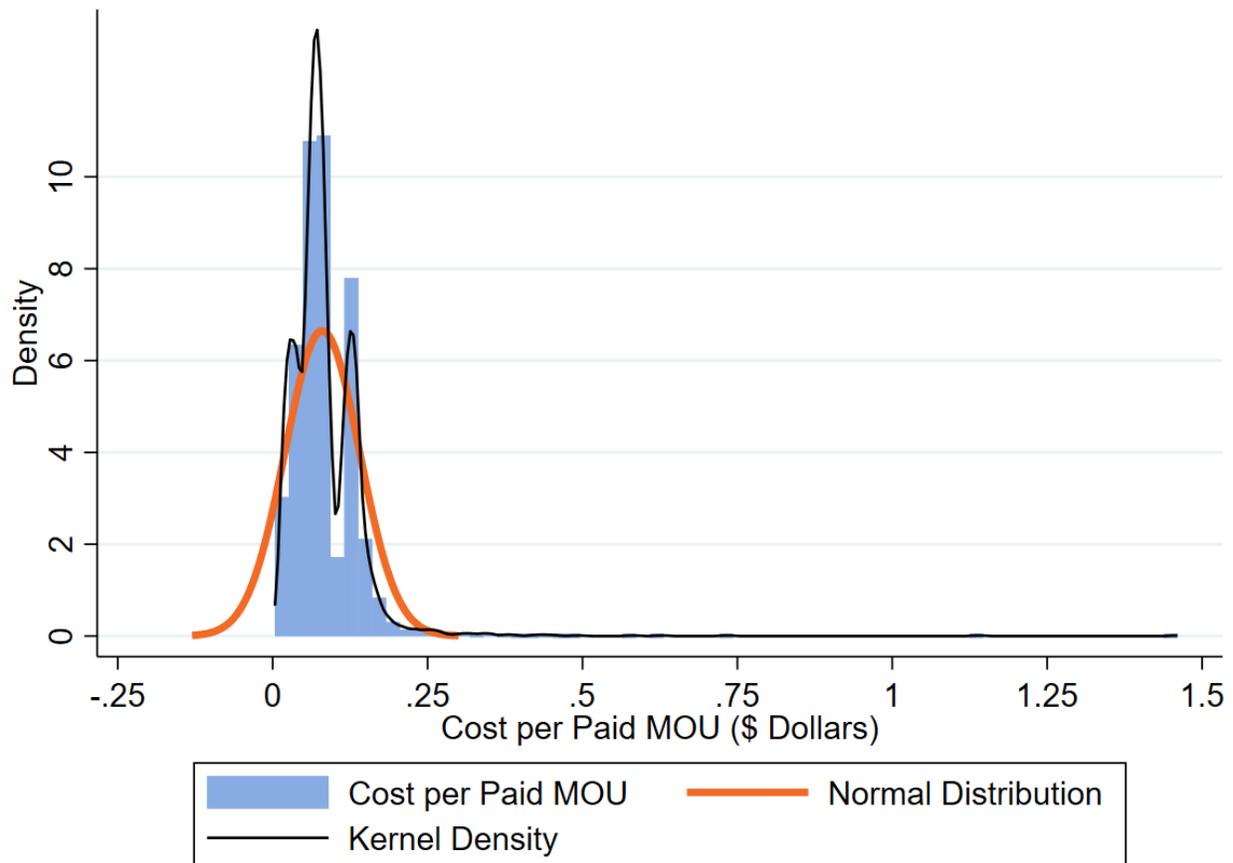
²² In the IP-Captioned Telephone Service rate setting context, Bazelon has argued against using the average cost as a basis for rate setting. See Coleman Bazelon and Brent Lutes, “Telecommunications Relay Services for Individuals who are Deaf or Hard of Hearing, in the FCC proceeding “Misuse of Internet Protocol (IP) Captioned Telephone Service; Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities,” CG Docket Nos. 13-24, 03-123, August 30, 2017.

²³ It is also largely unexplained. Variation that is clear in the data, such as jails versus prisons, is explicitly accounted for in rates.

²⁴ Skewness measures whether the data are symmetric. See NIST, “Engineering Statistics Handbook,” Measures of Skewness and Kurtosis, Chapter 1.3.5.11, April 2012, <https://www.itl.nist.gov/div898/handbook/eda/section3/eda35b.htm>, (“Engineering Statistics Handbook”).

than the left tail.²⁵ The implication of this is that the ICS data includes more observations of relatively small costs below the average cost and fewer observations of relatively higher costs above the average. Additionally, the data cannot be negative (they are ‘censored’ at zero) as these are cost figures. The differences between a theoretical normal distribution (with the same mean and standard deviation as the ICS cost distribution) and the current data are best seen in Figure 1.

FIGURE 1: COST PER MINUTE DISTRIBUTION COMPARED TO NORMAL DISTRIBUTION



Due to the skewed nature of the ICS cost distribution and the large variance, using inferences from the standard normal distribution, such as using the mean as a basis for a rate, would not be justified. The FCC’s addition of one standard deviation accounts for this skewness and reduces the amount of under-compensation to be within the norms of average cost based rate regulation. The magnitude of this adjustment is discussed in the next subsection.

²⁵ NIST, “Engineering Statistics Handbook.”

B. The Benefits of Using the FCC Metric

In a symmetric normal distribution, setting the rate at the mean cost would imply that half the providers will be under-compensated and half will be over-compensated.²⁶ 95% is a commonly used benchmark for what is acceptable with a random distribution of data.²⁷ Using that benchmark here to establish a rate would imply that only 5% of observations would not be fully compensated. Given the skewness of the data here – there are more smaller observations at very high costs than with normally distributed data – and using the mean plus one standard deviation to set the rate means only 7% of observations are not fully compensated.²⁸ Consequently, the FCC’s use of mean plus one standard deviation approximates the customary 95% benchmark. The rate of under-compensation is even lower when one calculates this rate using the FCC’s proposed rates of \$0.14 for prisons and \$0.16 for jails.

TABLE 1: COST PER MINUTE SUMMARY STATISTICS

| | All Data | Jails | Prisons |
|---------------------------------------|----------|---------|---------|
| Count | 2,935 | 2,804 | 131 |
| Mean | 0.0842 | 0.0839 | 0.0905 |
| Std. Dev. | 0.0608 | 0.0616 | 0.0401 |
| Mean + 1 Std. Dev. | 0.1450 | 0.1454 | 0.1306 |
| Variance | 0.0037 | 0.0038 | 0.0016 |
| Skewness | 7.5198 | 7.5823 | 0.1328 |
| Kurtosis | 130.510 | 129.931 | -0.822 |
| Mean as Rate Cap | | | |
| % of Observations Undercompensated | 36% | 35% | 52% |
| Mean + 1 Std. Dev. As Rate Cap | | | |
| % of Observations Undercompensated | 7% | 7% | 7% |
| FCC Proposed Rate as Rate Cap | | | |
| % of Observations Undercompensated | N/A | 5% | 6% |

Sources and Notes:

CONFIDENTIAL_Contracts_SubcontractorIndirectCostsIncluded_GTL100.xlsx

% of observation undercompensated is calculated as the number of contracts that fall above each rate cap as a ratio of the total number of contracts in that category.

An "All Data" ratio is not available under the FCC Proposed Rate because the FCC only specifies rates for each of jails and prisons.

²⁶ As seen in Table 1, in the overall ICS cost data 36% would be under-compensated if the rate was set at the mean.

²⁷ Adam Hayes, “Confidence Interval,” Investopedia, accessed January 15, 2021, <https://www.investopedia.com/terms/c/confidenceinterval.asp>.

²⁸ Given the likelihood that the reported costs are inflated, it is likely that for fewer than 7% of the observations the compensation would be less than *actual* costs.

The discussion above focuses on the number of observations that are over- and under-compensated. However, for a skewed distribution with a large variance, magnitude of such compensation is also important. In Table 2, we look at the magnitude of over- and under-compensation in terms of total costs and not observations. As can be seen, only 1% of total prison costs and 3% of total jail costs are not fully compensated based on the reported cost data under the FCC’s proposed rates, which is well below the accepted benchmark.

TABLE 2: UNDER-COMPENSATION AS A PERCENTAGE OF TOTAL COSTS

| | |
|---------------------------------|---------------|
| Prisons | |
| Total Cost | \$403,852,370 |
| Cost over Cap | \$4,937,939 |
| % of Total Cost Not Compensated | 1% |
| Jails | |
| Total Cost | \$293,468,435 |
| Cost over Cap | \$8,549,098 |
| % of Total Cost Not Compensated | 3% |

Sources and Notes:

CONFIDENTIAL_Contracts_SubcontractorIndirectCostsIncluded_GTL100.xlsx

Total cost is calculated as the sum of costs (where indirect costs are allocated by MOU) for each of prisons and jails.

'Cost over Cap' is calculated as the total cost above the FCC's proposed per-minute rate caps of \$0.14 for prisons and \$0.16 for jails.

'% of Total Cost Not Compensated' is calculated as the ratio of Cost over Cap over Total Cost.

IV. GTL’s Argument against the FCC’s Cost Adjustment is Incorrect

GTL takes issue with two of the Commission’s characterizations. First, it contends that ICS providers are non-dominant telecommunications providers and hence possess no market power. Second, it opposes the FCC’s use of the term “market rent,” and the resulting cost adjustment.²⁹ As we argue below, both contentions are unsupported.

²⁹ GTL Comments, Section II; GTL Economic Report, Section III.

A. Market Power Issue

GTL claims that the FCC has not established that it has market power, and therefore, any claims about market power are baseless. However, using standard techniques from competition economics, it is readily apparent that GTL, the largest provider, very likely has market power.

To study this, we use the Herfindahl-Hirschman Index (“HHI”), a commonly accepted market concentration measure.³⁰ The HHI is calculated as the sum of the square of market shares in a given market. This measure takes into account the relative size of the firms in a given market. The index approaches 0 when the market is occupied by many firms of equal size (low concentration) and increases as the number of firms decrease and the disparity between market share increases, eventually reaching 10,000 (100%²) in the case of monopoly.³¹ The DOJ considers an HHI below 1,500 points to be not very concentrated, between 1,500 and 2,500 points to be moderately concentrated, and in excess of 2,500 points to be highly concentrated.³²

Market share is typically calculated as the share of revenue in a market, although it can be calculated as the share of quantity of goods or services sold. We calculate it both ways. We calculated market shares based on paid minutes of use and revenue from the data provided in the Second Mandatory Data Collection. Table 3 below summarizes the share of total paid MOU and revenues for each ICS provider.

³⁰ The United States Department of Justice, “Herfindahl-Hirschman Index,” <https://www.justice.gov/atr/herfindahl-hirschman-index>.

³¹ The United States Department of Justice, “Herfindahl-Hirschman Index,” <https://www.justice.gov/atr/herfindahl-hirschman-index>.

³² Horizontal Merger Guidelines § 5.3 (2010).

TABLE 3: ICS PROVIDERS MARKET SHARE

| | Share of Paid MOU | Share of Revenue |
|-------------|-----------------------|---------------------|
| Prodigy | BEGIN CONFIDENTIAL [[| |
| GTL | | |
| Legacy | | |
| Securus | | |
| ATN | | |
| ICSI | | |
| CPC | | |
| Centurylink | | |
| Paytel | | |
| Correct | | |
| NCIC | | |
| Crown | | |
| Total | | |
| HHI | |]] END CONFIDENTIAL |

Sources and Notes:

CONFIDENTIAL_Contracts_SubcontractorIndirectCostsIncluded_GTL100.xlsx

Share of Paid MOU is calculated as the share of total paid MOU provided by each ICS provider.

Share of Revenue is calculated as the share of total ICS Revenue collected by each ICS provider.

HHI is calculated as the sum of the square of market shares.

Using the share of paid MOU as the basis for an HHI, the market for ICS is “highly concentrated” with an HHI of [[BEGIN CONFIDENTIAL]] *** [[END CONFIDENTIAL]]. Alternatively, measuring market share by ICS revenue results in an HHI of [[BEGIN CONFIDENTIAL]] *** [[END CONFIDENTIAL]] – also indicating a highly concentrated market. As economic literature has pointed out, in most cases, firms in a highly concentrated industry possess market power.³³

B. Cost Adjustment and Existence of Market Rents

GTL contends that the Commission’s cost adjustment is unwarranted and that there is no basis “to adjust GTL’s costs to reduce or eliminate the “distortion” caused by so-called “market rents.””³⁴ The Commission states that GTL’s costs were more than a third higher than that of the industry and even that of Securus, the other large ICS provider, and this is unexpected, given that its size would allow it to reap the benefits of economies of scale and thus actually have lower costs than smaller industry peers.³⁵ The FCC explains that a reason for the higher cost showing may be due to aspects of GTL’s cost measurement, particularly

³³ Oligopoly theory assumes “a positive relationship between market power and seller concentration.” Jeffrey Church and Roger Ware, “Industrial Organization, A Strategic Approach,” *Irwin McGraw-Hill*, p. 428.

³⁴ GTL Comments, p. 18.

³⁵ FCC, “FCC ICS 2020 FNPRM,” Appendix G, ¶ 1.

as it pertains to capital expenses incorporating market rents, and thus reduces its costs by 10% based on evaluating its financials.³⁶

The term market rent is used in the FNPRM when the FCC explains why it chose to discount GTL's cost:

"[T]o calculate the return component of its costs, GTL uses what it refers to as the "invested capital of GTL." That value equals the amount GTL's current owners paid in 2011 to purchase the company from its prior owners plus the amounts GTL paid for subsequent acquisitions. Those amounts as a matter of basic financial theory reflect GTL's estimate of the future profit streams the company would generate as an ongoing concern in the provision of inmate calling services and the other services GTL provides incarcerated people. Consequently, these prices include any expected market rents embodied in those profit streams. Use of GTL's invested capital as a basis for a regulated cost-based rate is inconsistent with the well-established principle that the purchase prices of companies that possess market power "are not a reliable or reasonable basis for ratemaking"³⁷

At issue here is the FCC assertion that GTL's inflation of reported costs is a result of including the cost of invested capital, which incorporate market rents, in its ICS service costs. In its costs, GTL has included "the cumulative total of the remaining unamortized value of "goodwill" associated with GTL's various acquisitions at different points in time."³⁸ GTL calculates goodwill of a newly bought asset as the difference between the purchase price and GTL's assessment of its fair market value (minus liabilities), and the FCC contends that this goodwill incorporates markets rents.³⁹

First, at the outset, with or without market rents, invested capital cost should not be included in the total cost for providing ICS. Working capital is a reasonable cost as it is related to funding ICS operations, not the acquisition of a company.⁴⁰ Second, in the event that the cost of invested capital is included, the FCC states that any incorporated market rents that are assigned to an asset, as a part of the company (compared to its standalone fair market value) should be discounted.⁴¹ For GTL, the 'goodwill' measure is one such entry on the balance sheet. Goodwill represents the amount paid for a company above the

³⁶ FCC, "FCC ICS 2020 FNPRM," Appendix G, ¶ 1.

³⁷ FCC, "FCC ICS 2020 FNPRM," ¶ 92.

³⁸ FCC, "FCC ICS 2020 FNPRM," Appendix G, ¶ 3.

³⁹ FCC, "FCC ICS 2020 FNPRM," Appendix G, ¶ 3.

⁴⁰ Penn Law, "An Aspect of Public Utility Rate Valuation: The Working Capital Allowance," Notes, accessed January 14, 2021. https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=7780&context=penn_law_review.

⁴¹ FNPRM, ¶¶ 92-93; Appendix G.

value of the assets it owns.⁴² When a company enjoys market rents, this is where that excess value often is recorded on a balance sheet. Thus, the FCC excludes goodwill-related expenses and adjusts GTL's costs downwards to account for this.⁴³

GTL argues that its capital costs appropriately include risk and depreciation, and while large, they cannot be associated with any one facility and the costs support “the business as a whole,” and that the “existence of market rents does not indicate market power.”⁴⁴ The existence of market power generally indicates the existence of rents associated with that market power.⁴⁵ We have shown that based on well-accepted measures of concentration GTL operates in a concentrated market environment which points towards the existence of market power, and hence associated rents. Therefore adjusting the cost downwards to discount these rents is appropriate.

V. The ICS Providers Misunderstand the Site Commission Allowance

In general, site commissions are defined as payments that ICS providers make to correctional facilities.⁴⁶ In the 2015 Order, the Commission provides a description of such payments.

“The record indicates that, in many cases, ICS bids are predicated on the winning providers’ willingness to share part of its ICS revenues with the correctional facility. These payments, commonly referred to as “site commissions,” may take the form of monetary payments, in-kind payments, exchanges, or allowances. In this Order, we define the term “site commission” broadly, to encompass any form of monetary payment, in-kind payment requirement, gift, exchange of services or goods, fee, technology allowance, product or the like.”⁴⁷

⁴² Jane G. Gravelle and Jack Taylor, “Tax Neutrality and the Tax Treatment of Purchased Intangibles,” *National Tax Journal* 45(1) March 1992, pp. 77-78.

⁴³ FCC, “FCC ICS 2020 FNPRM,” Appendix G, ¶¶ 3 – 7.

⁴⁴ GTL Comments, p. 19, 21, GTL Economic Report, ¶ 14.

⁴⁵ Jeffrey Church and Roger Ware, “Industrial Organization: A Strategic Approach,” *Irwin McGraw-Hill*, Section 2.4, “The ability of a firm to profitability raise price above marginal cost depends on the extent to which consumers can substitute to other supplies.” See also, Luís M. B. Cabral, “Introduction to Industrial Organization,” *The MIT Press*, p. 8.

⁴⁶ FCC, “FCC ICS 2020 FNPRM,” ¶ 100.

⁴⁷ FCC, “In the Matter of Rates for Interstate Inmate Calling Services,” Second Report and Order and Third Further Notice of Proposed Rulemaking, ¶ 117, WC Docket No. 12-375, adopted October 22, 2015, <https://docs.fcc.gov/public/attachments/FCC-15-136A1.txt>.

Site commissions can be potentially separated into two components: first, they can compensate correctional facilities for costs that they must “reasonably” incur when providing ICS services, and second, site commissions compensate correctional facilities for the transfer of market power from the facility to the ICS provider.⁴⁸ The purpose of the site commission allowance is not to compensate the ICS provider for the entire site commission paid. It would be inappropriate to compensate for the transfer of market power. Rather, it is designed only to compensate for the first component, to the extent it exists at all. As the FCC explains:

“The Commission has determined previously that some portion of these site commission payments do reflect legitimate costs that correctional facilities incur that are reasonably related to the provision of inmate calling services. Based on its analysis, the Commission’s proposed rate caps include a \$0.02 per minute allowance for these correctional facility costs.”⁴⁹

It is of course difficult to disentangle which part of the site commission payment goes towards reasonable costs and which portion is due to the transfer of market power. While the Commission could have chosen not to allow any compensation, due to data limitations on site commissions (the Second Mandatory Data Collection does not provide information as to the payments made for “reasonable” costs and the data only sheds light on the *total* commissions paid), it makes a reasonable attempt to estimate this first component and compensate ICS providers accordingly.

The FCC proposes a method that estimates the “legitimate costs that correctional facility incur that are reasonably related to the provision of inmate calling services.”⁵⁰ The FCC compares the total cost for facilities that do pay site commissions to those that do not. By calculating the difference, the FCC aims to isolate the gap in costs that could be covered by site commission payments. That is, as the FCC calculation shows, facilities that do not pay site commissions, in general, tend to have higher costs. The presumption is that this is because some of the inputs into providing ICS, such as some phone-related technology like call recording or other phone related equipment, may be provided in exchange for the site commissions.⁵¹ The ICS providers seem to misunderstand both the purpose and scope of the site commission allowance, and the FCC’s method for calculating the proposed allowance.

⁴⁸ FCC, “FCC ICS 2020 FNPRM, ¶ 100. It is worth noting that the market power noted here – exclusive access to the population of a particular facility – is distinct from the market power discussed in the previous section. Whether or not any providers possess market power in the market for ICS services, *all* providers have market power from the exclusivity of all ICS contracts.

⁴⁹ FCC, “FCC ICS 2020 FNPRM, footnote 209.

⁵⁰ FCC, “FCC ICS 2020 FNPRM, footnote 209.

⁵¹ The Commission holds that only the portion of the site commission that represents “legitimate correctional facility costs that are directly related to the provision of inmate calling services,” should be compensated. See FCC, “FCC ICS 2020 FNPRM, ¶ 103.

For example, GTL and Securus both calculate the average site commission across all contracts. GTL concludes that “site commissions are significantly higher than the \$0.02 allowance.”⁵² While GTL is correct in finding that the total site commissions paid exceeds the proposed allowance, this is because the total includes site commission payments that compensate correctional facilities for the transfer of market power from the facility to the ICS provider that should not reasonably be included in the cost base.

VI. The ICS Providers’ Comments Suggest that a Non-Allocated Cost Collection Approach May be Appropriate for Future Collections

The purpose of the Second Mandatory Data Collection is to collect data on the costs of providing ICS. Costs are separated into two main categories: direct costs (those costs that can be directly tied to ICS) and indirect, or overhead, costs (costs that are tied to ICS, but not directly). By nature, indirect costs are not associated with specific ICS contracts. Therefore, in order to calculate the per-contract cost the FCC allocated the indirect costs reported by each provider across all of the providers’ contracts. The FCC notes that the analysis was completed at the contract level because ICS providers reported that they do not report and record costs at the facility level.⁵³

The FCC used a cost allocation key based on the total paid minutes of use associated with each contract. That is, the agency assumed that common costs should be allocated in proportion to the number of paid minutes. The FCC also considered other cost allocation methodologies and explained why, in this case, those alternatives are not appropriate. The ICS providers take issue with the allocation key that the FCC adopted and propose alternatives. For example, Pay Tel and Securus claim that a direct cost allocation key would be appropriate while GTL argues that costs should be allocated according to revenue.⁵⁴ Issues of direct versus indirect and facility versus contract level costs can be discussed in greater detail in future data collections. However, these concerns are not a reason to delay rate setting by the FCC. The economic report filed by Securus illustrates how complicated such an analysis can become. Taking on the further complications suggested would only make sense if the information created was significantly more useful than the FCC’s current approach. Given the reasonableness of the FCC’s allocation of common costs by paid minutes of use, and the providers’ claims that total costs are accurate, we believe that the FCC has met its burden of demonstrating reasonableness in its allocation, and the ICS providers have not presented evidence sufficient to refute the Commission’s approach.

⁵² GTL Comments, p. 26.

⁵³ Note the same issues would exist with allocating common contract costs to individual facilities.

⁵⁴ Securus Economic Report, ¶ 24, Pay Tel Economic Report, p. 21, GTL Comments, p. 21.

Due to the variation in cost reporting and the concerns mentioned by the ICS providers about cost allocation, future FCC data collection might be better served by a total cost approach whereby the ICS providers report total cost (both direct and indirect) and no contract allocation is undertaken.

VII. Conclusion

This reply report addresses several claims made by the ICS providers and proposes ideas for any future ICS data collection by the FCC. As an initial matter, we address issues that were raised related to the data collection, methodology for the FCC's proposed rates, cost adjustments and cost allowances incorporated by the FCC in their proposed rates. Some ICS providers have criticized the FCC's data collection as inadequate and argued that the results of any analysis based on these data must be dismissed. We show that by their own admission, the current data that the Commission bases its rates on, are the best available and do not form a basis for objecting to the accuracy of the data or challenging the Commission's calculated rates. They also raise questions about the FCC finding that facility size does not have a significant impact on costs. We support the Commission's finding that facility size has no significant impact on costs and hence do not impact the proposed rates.

Another issue raised by the providers is the Commission's use of mean plus one standard deviation as a basis for proposing the rates. We analyze the ICS cost distribution, and show that given the variance and skewness of the distribution, the mean plus one standard deviation metric provides a similar magnitude of under-compensation as would be produced by using a mean plus two standard deviation metric in case of a symmetric normal distribution. In fact, the FCC metric is more conservative in terms of under-compensation than the mean plus two standard deviation approach that is used for a symmetric normal distribution. We show that only 1% of total prison costs and 3% of total jail costs are not fully compensated based on the reported cost data under the FCC's proposed rates, compared to 5% for a normal distribution evaluated at mean plus two standard deviations.

In this report, we also examine GTL's assertion that the FCC's cost adjustment is incorrect and refute the company's claim of no market power, and provide support for the FCC adjustment. Using the share of paid MOU and revenues, we calculate an HHI, and show that the market for ICS is "highly concentrated," and argue that in most cases, firms in a highly concentrated industry possess market power. Additionally, GTL also takes issue with the Commission adjusting its reported costs and lowering them by 10%, based on evaluating GTL's financials and concluding that a portion of the costs incorporated market rents. We support the cost adjustment and argue that the existence of market power generally indicates the existence of rents associated with that market power, and market rent should not be included in costs.

Additionally, we address the misunderstanding of the site commission allowance, and explain that the intent of the allowance was not to compensate for site Commissions, but to compensate for the portion

of the commission that may have been used to provide services related to ICS. Last, we propose a simplification of the data collection for future proceedings.