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Jon Wilkins
Chief, Wireless Telecommunications Bureau
Federal Communications Commission
445 12th Street, SW
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Dear Mr. Wilkins:

AT&T takes sharp issue with the Wireless Telecommunications Bureau's preliminary conclusions regarding Data Free TV. Data Free TV is precisely the kind of pro-consumer initiative this Commission should be encouraging. It delivers real value to consumers and provides another video streaming alternative to cable. Other video providers can be expected to respond to this innovation either by sponsoring their own content with AT&T and/or other wireless providers or by finding different ways to improve and differentiate their offerings and generate consumer value. Indeed, they have already begun to do so. And just this morning, T-Mobile intensified wireless competition in response to Data Free TV by offering AT&T customers a free year of DIRECTV NOW if they switch to T-Mobile—the equivalent of a $35 monthly discount.[1] This is the competitive process at work, driving innovation, lowering prices, and increasing consumer value.

The Bureau's most recent letter accepts, as it must, that Data Free TV offers consumers enormous value at low prices.[2] More than three million customers have enjoyed the benefits of Data Free TV in the short time since DIRECTV made it available. The latest iteration of the service, DIRECTV NOW, offers consumers attractive packages of TV channels that they can watch on any device for as little as $35 a month with no annual contract, no credit check, no installation, and no set-top box. But the consumer appeal of this service is paradoxically what underlies the Bureau's "preliminary conclusion" that AT&T should be condemned for offering it. In the Bureau's view, the very attractiveness of Data Free TV makes life too hard on DIRECTV's video rivals when they compete for AT&T mobile customers, *see 12/1 Letter* at 2, even though AT&T's sponsored data program is available to those rivals at the same low wholesale rate that DIRECTV pays.

The Bureau's approach thus would deny consumers a service they value, raise prices, lower consumption, and curb the disruptive potential of Data Free TV, all in the name of preserving profit margins for individual DIRECTV rivals. That approach would upend the most basic principles of American competition policy, which is designed for "the protection of

[1] Press Release, *T-Mobile Offers DIRECTV NOW for FREE* (Dec. 15, 2016), https://newsroom.t-mobile.com/news-and-blogs/directv-now-offer.htm.

[2] Letter from Jon Wilkins, FCC, to Robert Quinn, AT&T (Dec. 1, 2016) ("*12/1 Letter*").

competition, not competitors."[3] And it also would scrap decades of regulatory precedent making clear that even a monopolist may provide downstream services to an affiliate as long as those services are available to others on the same terms. Because the Bureau's proposal would represent such a radical departure from settled law, the Bureau has no authority to inflict this agenda on American consumers, as Commissioners Pai and O'Rielly have explained. Any "final conclusions" the Bureau may purport to draw against Data Free TV (*12/1 Letter* at 3) would thus be unenforceable.

DISCUSSION

I. The Bureau Does Not Defend Its Original Proposal For A Broad Presumption Against Charging Third Parties For Telecommunications Inputs That A Common Carrier Also Provides To Its Edge Affiliate.

The Bureau has still articulated no plausible basis for challenging Data Free TV as "anticompetitive." Its prior letter suggested that any sponsored data program would be inherently discriminatory if a wireless provider charged third parties *anything* for inputs that it provides to its edge-services affiliate while incurring "no cash cost on a consolidated basis."[4] As we explained, that position conflicts with congressional policy and 35 years of Commission precedent. Since *Computer II*, the Commission has entitled common carriers to provide edge services so long as they offer to sell telecommunications inputs to unaffiliated edge providers on nondiscriminatory terms—even though, by purchasing those inputs, the unaffiliated provider would necessarily incur "cash costs" that the vertically integrated company would not incur "on a consolidated basis."[5] Likewise, Congress entitled any Bell operating company to charge unaffiliated long distance companies for local access services on the same nondiscriminatory terms that it sold those services to its own long distance affiliate or imputed to itself. *See id.* at 6. The logic of the prior Bureau letter—that common carriers must give away telecommunications inputs for free to meet the requirements of Title II—is both irreconcilable with that precedent and nonsensical.

Rather than deny this point, the Bureau responds with irrelevant quibbles. It first objects that the Commission originally required "structural separation … between the telecommunications carrier and the edge affiliates." *12/1 Letter* at 3. That point is doubly inapposite. First, the Commission eliminated the *Computer II* structural separation requirement in *Computer III*,[6] and it allowed the section 272 separation requirements to sunset precisely

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[3] *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (emphasis omitted).

[4] Letter from Jon Wilkins, FCC, to Robert Quinn, AT&T, at 2 (Nov. 9, 2016) ("*11/9 Letter*").

[5] *See* Letter from Robert Quinn, AT&T, to Jon Wilkins, FCC, Legal Analysis at 5-9 (Nov. 21, 2016) ("*AT&T 11/21 Legal Analysis*").

[6] *See, e.g.*, Mem. Op. & Order, *EarthLink, Inc. v. SBC Commc'ns*, 31 FCC Rcd 4311, 4317-18 ¶ 16 (EB 2016) ("*EarthLink Order*") ("For many years, the Commission required the complete structural separation of the [Bell operating companies'] enhanced services operations from their regulated common carrier operations in order to discourage cross-subsidy. The Commission then moved away from structural separation requirements in favor of nonstructural safeguards, which it found would allow the BOCs to provide enhanced services more efficiently.") (footnote omitted) (citing Report & Order, *Amendment of*

because they were unnecessary to prevent discrimination.[7] Second, and in any event, DIRECTV *is* a separate affiliate of AT&T.

The Bureau next observes that the Commission imposed "accounting safeguards and cost allocation requirements" when local telephone companies provided edge services of their own. *12/1 Letter* at 3. That too is irrelevant. Such micromanagement was necessary only because those telephone companies were price-regulated *monopolists* and thus had both the incentive and the ability to harm competition in unregulated downstream markets—for example, by misallocating costs to local exchange services in order to cross-subsidize their unregulated services.[8] Here, neither AT&T Mobility nor DIRECTV is even the leading provider in any relevant telecommunications market, let alone a monopolist, and neither is subject to prescriptive rate regulation.[9] The purpose of the cost-allocation rules is thus not even implicated here. Indeed, broadband competition is a key reason why the Commission has forborne from (or refused to impose) the *Computer Inquiry* rules in any broadband Internet access market, a point the Bureau also ignores.[10]

More fundamentally, the Bureau's error-ridden references to regulatory history have no bearing on our basic point. The Bureau's original letter proposed a bright-line prohibition on any

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Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 104 F.C.C. 2d 958, 1063-70, ¶¶ 210-225 (1986)).

[7] *See* 47 U.S.C. § 272(f)(2).

[8] *See, e.g.*, Joseph Farrell & Philip J. Weiser, *Modularity, Vertical Integration, and Open Access Policies: Towards a Convergence of Antitrust and Regulation in the Internet Age*, 17 HARV. J. L. & TECH. 85, 105-107 (2003) (explaining that price regulation can give platform monopolists otherwise nonexistent incentives to discriminate against rival providers of complementary applications).

[9] In a bizarre "reverse leveraging" theory, the Bureau suggests that AT&T Mobility launched this program to "preserve [AT&T/DIRECTV's] already leading position in the market for multi-channel video services[.]" *12/1 Letter* at 3. This makes no economic sense. First, the relevant DIRECTV services constitute only a small fraction of the total video streamed online, and DIRECTV appears in that context as a new entrant, not an incumbent. In any event, even if it is appropriate to view those services as part of a larger MVPD product market, the "relevant geographic market" for MVPD services is the "local market in which consumers select MVPD services" and, specifically, "the franchise area of the local cable operator." Mem. Op. & Order, *Applications of Charter Commc'ns, Inc., Time Warner Cable Inc., and Advance Newhouse P'ship*, 31 FCC Rcd 6327, 6399 ¶ 153 (2016) (citing cases); Mem. Op. & Order, *Gen. Motors Corp. & Hughes Elecs. Corp.*, 19 FCC Rcd 473, 505 ¶ 62 (2004). It thus makes no difference which company has more customers *nationwide*; the competitive question is which company has market power within particular geographic markets. The answer is the cable incumbent. On average, cable still controls more than half of each local market, and the two satellite providers *combined* typically account for only about a third. *See* 17th Report, *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 31 FCC Rcd 4472, 4501-02 ¶ 73, Table III.A.5 (2016).

[10] *See* Report & Order, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14,853, 14,875-98 ¶¶ 41-85 (2005), *aff'd sub nom. Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205, 220-222 (3d Cir. 2007); *see also* Declaratory Ruling, *Appropriate Regulatory Treatment for Broadband Access to the Internet over Wireless Networks*, 22 FCC Rcd 5901, 5914 ¶ 34 (2007).

sponsored data program that requires unaffiliated edge providers to pay *anything* for the same transmission inputs that a mobile carrier provides to its edge services affiliate, reasoning that it is inherently "discriminatory" to impose *any* "cash cost" on an unaffiliated company when the vertically integrated company incurs "no cash cost on a consolidated basis." *11/9 Letter* at 2-3. Thirty-five years of Commission precedent foreclose that position.

II. The Bureau Articulates No Cognizable "Price Squeeze" Claim.

The Bureau's December 1 letter understandably deemphasizes its broad-brush attack on charging third parties anything for telecommunications inputs and focuses instead on a more fact-specific claim: that third-party video providers would find it "very difficult" to pay AT&T's particular sponsored data rate while "competing for AT&T Mobility customers" who currently enjoy "DIRECTV Now's $35 retail price." *12/1 Letter* at 2. Although the Bureau resists using the term, this is a classic "price squeeze" argument—*i.e.*, an argument that a vertically integrated firm has "squeeze[d] its downstream competitors by raising the wholesale price of inputs while cutting its own retail prices."[11] In particular, the Bureau is claiming that the retail prices for DIRECTV NOW are so low, relative to the cost of sponsored data, that unaffiliated providers could not profitably compete with DIRECTV NOW on AT&T's mobile network.

This price squeeze claim is untenable. As an initial matter, the Bureau claims not to be questioning DIRECTV's retail rates, and for good reason: the Commission has held for nearly three decades that "[t]he pricing of individual nonregulated products and services"—here, DIRECTV NOW—"does not fall within our statutory mandate. Complaints about predatory pricing in nonregulated markets are the province of antitrust laws."[12] "Applying this precedent," the Commission has repeatedly "rejected arguments that a nonregulated service failed to recover its costs, thereby distorting the market for the service."[13] More generally, the Commission lacks statutory authority to "review the costs of particular nonregulated activities for purposes of establishing a relationship between cost and price."[14]

In any event, although the Bureau refers only to the $35 introductory rate for one DIRECTV NOW package, the actual rates for this service will vary, both from bundle to bundle and over time. For example, DIRECTV is offering its standard 100+ channel package at $35 for early adopters, but the standard rate for that package is $60. The Bureau ignores that fact when suggesting that the actual prices DIRECTV charges for these services are somehow predatory. And it is black-letter law that such promotional prices cannot form the basis of a predatory pricing claim.[15]

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[11] *Pac. Bell Tel. Co. v. linkLine Commc'ns, Inc.*, 555 U.S. 438, 449 (2009).

[12] Report & Order, *Separation of Costs of Regulated Tel. Serv. from Costs of Nonregulated Activities*, 2 FCC Rcd 1298, 1304, ¶ 40 (1987) (quoted in *EarthLink Order* ¶ 19).

[13] *EarthLink Order* ¶ 20.

[14] *Id.* ¶ 23.

[15] *See, e.g.*, *American Acad. Suppliers, Inc. v. Beckley-Cardy, Inc.*, 922 F.2d 1317, 1322 (7th Cir. 1991) (Posner, J.); Order on Recon., *Int'l Settlements; Policy Reform Int'l Settlement Rates*, 20 FCC Rcd

Because the Bureau does not claim that DIRECTV services are priced too low, the only way it might establish a predicate for a notional price squeeze claim would be to show (among other things) that AT&T Mobility is somehow able to charge a supra-competitive rate for sponsored data. The Bureau does not even purport to make such a showing. To the contrary, it accepts *arguendo* that the sponsored data rate is as low as the lowest wholesale rate paid by the largest wireless resellers who make the greatest volume commitments, while questioning the "relevance of" this comparison. *12/1 Letter* at 2 n.5. But its relevance is straightforward. The wholesale rate benchmark is the product of intense competition among all facilities-based wireless carriers for the business of the largest resellers. Tellingly, the Bureau proposes no alternative methodology for calculating an appropriate sponsored data rate.

Nor does the Bureau address how AT&T/DIRECTV could possibly benefit from a predatory pricing strategy. Neither AT&T Mobility nor DIRECTV is or could conceivably become a monopolist in any relevant market. Thus, neither could charge predatory prices in the short term in the hope of recouping monopoly profits in the long term. *See 11/21 AT&T Legal Analysis* at 11-12. Without the likelihood of recoupment, a price squeeze strategy is completely irrational. The Bureau simply ignores that basic consideration.

In addition, the Bureau ignores a number of other material facts, all of which undermine its competitive analysis. First, unaffiliated providers are free to manage costs by buying as much or as little sponsored data as they choose. Second, other wireless carriers offer their own sponsored data programs that unaffiliated video providers can and do use. Third, sponsored data is only one of many means by which video providers can differentiate their products and compete for customers, and other providers of video services have, or can be expected to develop, their own ways of delivering consumer value in the marketplace. Finally, consumers unhappy with AT&T's choice of sponsored data partners can switch to other carriers in this highly competitive market, in which AT&T is not even the leading provider, let alone a monopolist.

III. Pulling the Plug on Data Free TV Would Affirmatively Harm Consumers.

Although the Bureau implicitly concedes that Data Free TV offers substantial consumer value, the Bureau ignores the many ways in which consumers would be substantially worse off if DIRECTV were forced to discontinue this program. First, because the sponsored data rate is far below the level of typical retail rates, the program allows consumers to purchase more data for less money than if they had to pay for their increased usage directly through higher per-unit retail charges. *See 11/21 AT&T Legal Analysis* at 3, 8. Thus, pulling the plug on that program would result in consumers purchasing *less* data for *more* money. For example, the Bureau suggests that AT&T should eliminate its sponsored-data program so that any DIRECTV competitor will find it more commercially feasible to "require its customers to pay significant amounts for their own usage of data" on AT&T's mobile network. *12/1 Letter* at 2. But consumers would be the losers in that scenario, and the only winner would be DIRECTV's competitor, which would benefit at

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14,106, 14,114 ¶ 21 n.60 (2005) ("Even if [prices suggesting a price squeeze were in place], there may be alternative explanations for such pricing, e.g., limited-time promotions to gain market share.").

consumers' expense from this regulatory price umbrella. The Bureau makes no response to that point, which we stressed in our initial submission.

The Bureau likewise ignores our observation that this sponsored data arrangement is at least as desirable from a competition policy perspective as a bundled rebate program in which DIRECTV sends consumers a monthly check to cover the retail rates they pay AT&T for the mobile usage attributable to DIRECTV streaming. *See 11/21 AT&T Legal Analysis* at 8-9. No one would doubt that such a rebate program would be pro-consumer. Indeed, it is precisely the type of vertical-integration efficiency that the Commission lauded in approving AT&T's 2015 merger with DIRECTV. *Id.* Moreover, AT&T's sponsored data arrangement with DIRECTV is in fact economically superior to the hypothetical rebate arrangement because, again, the rates DIRECTV pays AT&T for sponsored data are lower than the retail data rates consumers would otherwise pay AT&T, with the result that consumers pay less for more. *Id.* The Bureau makes no response to that point, and there *is* no response. Whatever the Internet conduct standard may mean, it cannot support this irrational exaltation of form over economic substance.

Terminating the sponsored data program would also weaken DIRECTV NOW's potential to disrupt the cable-dominated pay-TV marketplace. Consumers are more likely to perceive DIRECTV NOW as a cable substitute if, as with cable, they can consume as much of it as they like without worrying about overages. The Bureau's attack on Data Free TV, if successful, would accordingly make consumers less likely to view DIRECTV NOW as a cable substitute and thus blunt the competitive pressure this program imposes on cable incumbents.

The Bureau completely ignores that anticompetitive impact when it claims that pulling the plug on Data Free TV is somehow necessary to promote what it calls a "virtuous cycle." *12/1 Letter* at 1. The only virtuous cycle that benefits consumers—as opposed to individual competitors—is one in which each provider uses whatever advantages it may have to undercut the competition, and every other provider feels compelled to respond to attract and retain customers. For example, AT&T's exclusive agreement to distribute the earliest iPhones helped both AT&T and Apple, and the iPhone's success in turn inspired others to partner with Google in developing the rival (and now leading) Android platform.

Likewise here, AT&T and DIRECTV have used the advantages of integration to intensify both wireless and video competition. Cable companies will respond by leveraging their own advantages, such as faster broadband connections, and can be expected to offer their own mobile video products, as they have vowed to do.[16] They and other video competitors can pursue sponsored data arrangements with other wireless carriers. And T-Mobile has already reacted to Data Free TV by offering a free year of DIRECTV NOW to AT&T wireless customers who

[16] *See, e.g.*, *11/29 Recode Article*, *supra* ("[N]ow that AT&T's in the market, expect more of the traditional TV guys to follow suit. Comcast, for instance, has been mulling a service like this for years."); *see also* Shalini Ramachandran & Ryan Knutson, *Comcast to Launch Wireless Service by Mid-2017*, Wall St. J. (Sept. 20, 2016), http://www.wsj.com/articles/comcast-to-launch-wireless-service-by-mid-2017-1474378548 ("Comcast Corp. Chief Executive Brian Roberts said Tuesday the cable giant is aiming to launch a wireless service by mid-2017, creating a new line of business that could help the company better retain cable customers in a fiercely competitive pay-TV market.").

switch to T-Mobile. This is the essence of competition. If the Internet conduct standard banned such competition, which it does not, this "investigation" would supply yet another reason to abolish it.

IV. The Bureau Lacks Delegated Authority To Challenge Data Free TV.

As we previously explained, the Bureau may not take unilateral action against Data Free TV because doing so would contradict existing Commission precedent and because the Bureau lacks delegated "authority to act [in matters] present[ing] new or novel questions of law or policy which cannot be resolved under outstanding Commission precedents and guidelines." 47 C.F.R. § 0.331; *see 11/21 AT&T Legal Analysis* at 12-14. The Bureau's December 1 letter (at 3) implies once again that the totality-of-the-circumstances "Internet conduct standard," with its nonexclusive seven factors, somehow prohibits this program and leaves no room for policy discretion. That position is untenable, as the Internet conduct standard prescribes no clear rules of any kind. *See 11/21 AT&T Legal Analysis* at 13.

Any doubts on that score were put to rest when two FCC Commissioners, both of whom will remain in office after the imminent change of administration, criticized this investigation and warned the Bureau against unlawfully usurping core policymaking powers that only the Commission may exercise.[17] Those Commissioners also observed that whatever judgment the Bureau purports to pass on this program before January 20 will very likely be reversed shortly thereafter. Their remarks confirm that the Bureau lacks delegated authority to pull the plug on Data Free TV and disrupt service to the millions of customers who now enjoy that feature.

We trust that the Bureau will acknowledge that point and await further action by the Commission itself.[18]

Sincerely,

Joan Marsh

[17] *See* Statement of Commissioner Ajit Pai (Dec. 2, 2016) (condemning "[t]his end-run around Congress's clear instruction" against deciding "complex, partisan, or otherwise controversial items"); Statement of Commissioner Michael O'Rielly on FCC's Zero-Rating Investigation (Dec. 2, 2016) ("[i]t would be difficult to come up with a better example of a complex, controversial policy at the current Commission than this attempt to intimidate providers in order to shut down popular offerings to consumers").

[18] The 12/1 Bureau Letter (at 5) asks AT&T to answer highly fact-specific questions about the operation of Data Free TV, such as "[w]hat monthly usage levels" the typical DIRECTV NOW subscriber consumes and how much time he spends "streaming or downloading video via Wi-Fi rather than cellular networks." Of course, because DIRECTV NOW became available to consumers only on November 30, it is far too early to provide useful data of this kind.