KELLEY DRYE & WARREN LLP
A LIMITED LIABILITY PARTNERSHIP

WASHINGTON HARBOUR, SUITE 400
3050 K STREET, NW
WASHINGTON, D.C. 20007-5108

(202) 342-8400

NEW YORK, NY
TYSONS CORNER, VA
CHICAGO, IL
STAMFORD, CT
PARSIPPANY, NJ

BRUSSELS, BELGIUM

AFFILIATE OFFICES
JAKARTA, INDONESIA
MUMBAI, INDIA

FACSIMILE
(202) 342-8451
www.kelleydrye.com

DIRECT LINE: (202) 342-8518
EMAIL: tcohen@kelleydrye.com

REDACTED - FOR PUBLIC INSPECTION

February 5, 2016

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

VIA ECFS

Re: Comments of XO Communications, LLC on the ILECs' Direct Cases – WC Docket No. 15-247

Dear Ms. Dortch:

XO Communications, LLC ("XO"), through its attorneys, hereby submits comments on the ILECs' Direct Cases pursuant to the Investigation Order in the above-referenced proceeding. The submission contains Highly Confidential Information. In accordance with the Order and Protective Orders in this proceeding (DA 15-1387), this filing consists of a redacted copy of XO's submission to the Commission.

Copies of the Highly Confidential version of the filing are being submitted to the Secretary's Office and Commission staff via hand delivery under separate cover.

Sincerely,

Thomas Cohen

Thomas W. Cohen
Edward A. Yorkgitis, Jr.
Kelley Drye & Warren LLP
3050 K Street, NW, Suite 400
Washington, DC 20007
Tel. (202) 342-8540
Fax. (202) 342-8451

Counsel for XO Communications, LLC

**HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO
PROTECTIVE ORDERS IN WC DOCKET NO. 15-247
BEFORE THE FEDERAL COMMUNICATIONS COMMISSION**

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the Matter of: Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plan	WC Docket No. 15-247

COMMENTS OF XO COMMUNICATIONS, LLC ON ILECS' DIRECT CASES

Lisa R. Youngers
XO Communications, LLC
13865 Sunrise Valley Drive
Herndon, VA 20171
Telephone: (703) 547-2258

Thomas W. Cohen
Edward A. Yorkgitis, Jr.
Kelley Drye & Warren LLP
3050 K Street, NW, Suite 400
Washington, D.C. 20007
Telephone: (202) 342-8400
Its Attorneys

February 5, 2016

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247
BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

SUMMARY

This Bureau's tariff investigation into certain term and volume discount plans of Verizon, AT&T, Frontier, and CenturyLink for DS1 and DS3 special access (collectively, the "Discount Plans") is a necessary complement to the Commission's contemporaneous Special Access Rulemaking proceeding. XO Communications, LLC's ("XO") demonstrated in its comments in the Rulemaking that in most areas of the country, markets for Dedicated Services (e.g., TDM-based DSn special access and packet-based dedicated services, such as Ethernet) are not competitive. This results in the incumbent local exchange carriers ("ILECs") being able to charge supra-competitive prices. Further, ILECs have extended their market control by locking-up potential demand through the Discount Plans under investigation and by engaging in price squeeze behavior. Consequently XO demonstrated that the Commission needs to adopt and apply new triggers for deregulation of Dedicated Services and to reregulate prices in areas subject to pricing flexibility under the now suspended regime where markets are not competitive. Further, XO submitted that the Commission should adopt interim prices for ILEC Dedicated Services that are just and reasonable based on the lowest prices the ILECs offer today. Those prices are not based on economies of scale.

In this special access tariff investigation, context is critical. The retail Dedicated Services market, including for DSn service, is not competitive, except in limited, dense areas with substantial customer spend and where there is facilities-based competitive presence in or, in some cases, near buildings. Even in the areas where the market for DSn connections is competitive, because many customers have requirements for access at multiple locations,

competitors must obtain access to other locations many of which are outside competitive pockets.

To bring competition to retail customers relying on DS1 (or DS3) connections, XO needs access to ILEC unbundled network elements ("UNEs") and special access services. However, the FCC has reduced access to UNEs in many areas, and the ILECs are phasing out copper loops, the key UNE facility. Further, ILECs have priced wholesale access to special access services at high rack (month-to-month) rates, which means that XO, as a general matter, cannot use them economically to compete. As a result, , to get wholesale access to services at rates that begin to allow XO to compete, it has no option other than purchasing under the ILEC Discount Plans.

XO has been a customer under ILEC Discount Plans for many years and recently renewed its plans with Verizon and AT&T. But the ILEC Discount Plans under investigation, especially those of AT&T and Verizon, effectively required XO to commit substantial portions of its demand for DSn channel termination circuits on renewal and enforced that commitment through the imposition of onerous penalties. Because it would incur unreasonable shortfall penalties at the end of the Discount Plan terms that were expiring, XO was unable to migrate users at the time of renewal – at all in the case of Verizon (North and South, in particular) and to a significant degree in the case of AT&T. Consequently, large volumes of DS1 channel terminations and, in the case of Verizon, DS3 special access channel terminations, remain committed under multi-year agreements. All of this is happening in a marketplace where demand for DS1 and DS3 services are declining, greatly increasing the pernicious nature of the

Discount Plans. In short, once it signed up under the Discount Plans, XO has had no effective choice as to how many circuits it commits.

When the foregoing elements are combined, these ILEC agreements lock-in CLEC demand. As a result, XO and other CLECs limit their deployment of new facilities.

In their Direct Cases, Verizon and AT&T claim that participation in the Discount Plans under investigation is voluntary and that the shortfall penalties contained in these Discount Plans merely reflect "the benefit of the bargain" that CLECs make with ILECs for receiving discounts from the ILEC's rack rates without early termination liability. However, given ILEC market power in commercial buildings in most locations and the high rack rates of the ILECs for DS1 and DS3 services, XO's participation in Discount Plans is anything but voluntary. The ILEC's Discount Plans are not the result of any bargain between XO or other CLECs and the ILECs, and XO's entry into the ILEC Discount Plans is not voluntary in any normal sense of the word.

Given these circumstances, it becomes plain that the Discount Plans of Verizon North and South and those of AT&T are unjust and unreasonable, in violation of Section 201(b) of the Communications Act. The percentage based minimum commitments and shortfall penalties are the principal culprits. Neither Verizon nor AT&T have offered any supportable basis for the minimum commitment levels included in the Discount Plans, nor can they acknowledge provide the basis for setting the percentages in the first place. Because the Discount Plans of Verizon and AT&T lock-in large volumes of demand upon Plan renewal in a market where demand is declining, backed by high shortfall penalties, without any cognizable justification, they should be declared unjust and unreasonable.

Moreover, the shortfall penalties in many of the Discount Plans under investigation are unjust and unreasonable. Different Discount Plans structure the shortfall penalties in such different ways and at different levels, yet the same thin justification is offered for all of them: to ensure the ILEC receives the benefit of the bargain. While certain of the ILEC's shortfall penalties are directly tied to full "expectation damages," others are only a small fraction, and yet others, the penalties of Verizon North and South, Southwestern Bell, and PacBell have been, or have the capability to be, multiple times the cost of the channel terminations XO would have to purchase to make up the minimum commitment shortfall. This great variability of approaches and impact on Discount Plan customers when there is a shortfall reveals the shortfall penalties set at higher levels, including full expectation damages, to be arbitrary and unwarranted. The penalties that have been imposed by Verizon North and South on XO, for example, are grossly disproportionate to full expectation damages – two to three times higher – because they are based on unwarranted assumptions of purchases of interoffice transport (mileage and MUXing charges) that are unrelated to the minimum commitments XO has made. Despite the high levels of the penalties, neither Verizon nor AT&T can justify them The shortfall penalties based on full expectation damages or higher serve to lock-in XO's demand and prevent XO from moving demand for Dedicated Services to competitive providers and even its own network. These shortfall penalties are unjust and unreasonable.

In sum, the Commission should grant relief to ensure that special access DS1 and DS3 services are available on just and reasonable terms, by holding that the percentage minimum commitment provisions and the shortfall penalty provisions of Verizon North and South and

AT&T under its four Discount Plans to be void and unenforceable. At the same time, the Commission, in the Special Access Rulemaking, should conclude that the month-to-month "rack" rates for Dedicated Services, except where XO's proposed new triggers for pricing flexibility have been met, should be reset at the lowest rate available under the Discount Plans. Finally, in light of the marketplace changes as DSn service demand declines and the demand for packet-based dedicated services increases, wholesale customers under a Discount Plan should be able to move circuits out of the Plan to Ethernet services, UNEs, a customer carrier's own facilities, or to those of an alternative provider.

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Before the
FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of: Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plan	WC Docket No. 15-247

COMMENTS OF XO COMMUNICATIONS, LLC ON ILECS' DIRECT CASES

XO Communications, LLC ("XO") hereby submits comments in response to the ILECs' Direct Case submissions as required by the Designation Order in the above-referenced proceeding.[1] As explained herein, certain terms and conditions of the incumbent carrier's tariffs that are the subject of the Commission's investigation are unjust and unreasonable in violation of Section 201(b) of the Communications Act. The Commission therefore should declare these terms and conditions to be unlawful.

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[1] *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plan*, WC Docket No. 15-247, Order Initiating Investigation and Designating Issues for Investigation, DA 15-1194 (rel. Oct. 16, 2015) ("Designation Order").

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I. XO AND OTHER COMPETITORS LACK CHOICE OF WHOLESALE PROVIDERS AND MUST RELY ON INCUMBENT LOCAL EXCHANGE CARRIER FACILITIES AND SERVICES

A. Retail commercial consumers by and large lack facilities-based competitive choices for Dedicated Services.

As set forth in XO's just-filed comments in response to the *Special Access NPRM*,[2] despite Congress and the regulators promoting competitive entry for two decades, small, medium, and large businesses as well as enterprise users generally do not have a choice of local exchange carriers providing Dedicated Services.[3] Instead, incumbent local exchange carriers ("ILECs"), with their ubiquitous network presence and pervasive relationships with consumers, building owners, and local governments, continue to dominate the provision of Dedicated Services in virtually all locations around the country. This holds for the still substantial numbers of retail commercial customers with lower performance needs who continue to access TDM-based services over ILEC facilities (regardless of whether they purchase directly from an ILEC or from a competitive local exchange carrier ("CLEC") that acquires the facilities or services from the incumbent at wholesale). It also holds for customers who use higher performance

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2 *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, *AT&T Corporation Petition for Rulemaking Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593, Report and Order and Further Notice of Proposed Rulemaking, 27 FCC Rcd 16318 (rel. Dec. 18, 2012). *Comments of XO Communications, LLC on the Further Notice of Proposed Rulemaking*, WC Docket No. 05-25, RM-10593 (Jan. 27, 2016) (hereafter, "XO's *Special Access NPRM* Comments").

3 As used throughout, "Dedicated Services" refers to circuit and packet-switched services, e.g., Time Division Multiplexing ("IDM") services, such as DS1s and DS3s, and Ethernet services, respectively.

Ethernet services because CLECs either use ILEC facilities or services or have only been able to economically deploy fiber to a relatively small number of commercial buildings in select areas.[4]

The continued market power of ILECs should not be surprising. After all, the incumbents took many decades to build their networks. They had the advantage of being a government-sanctioned monopoly with a guaranteed return on their investments. And when statutory marketing opening provisions designed to end that local monopoly were passed in 1996, they started the "competitive era" with a nearly 100% market share and other advantages competitors lacked. In contrast, to break that monopoly power, not only must competitors raise enormous amounts of capital to build network facilities, they must obtain public and private rights-of-way ("ROW") and access rights to buildings, engage in expensive and time-consuming construction projects to build metro facilities and laterals to locations, and market to and sign up customers – all without a guaranteed rate of return. Having learned the lessons from the network deployment decisions of the post-1996 Telecommunications Act "boom" era, competitive providers today do not deploy facilities, including laterals to commercial buildings, on speculation. Rather, XO, as a rule, constructs laterals only after it has signed up subscribers with

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[4] As discussed below and noted in XO's *Special Access NPRM* Comments, XO and other competitors use TDM facilities and service to provide Ethernet services, in addition to offering them over their own facilities and reselling finished ILEC Ethernet services. Using TDM DS0 copper loops, XO provides Ethernet over Copper ("EoC") services from lower speeds up to 20 Mbps, and occasionally as high as 100 Mbps. XO's *Special Access NPRM* Comments at 17. DS1 and DS3 special access facilities can be used to provide Ethernet over Serial ("EoS") services, typically at speeds of 3-4.5 Mbps and up to 10 Mbps using DS1s, and speeds of 44 and 88 Mbps using DS3s.

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a sufficient spend, and, even then, it must complete installation and provide service in a timely manner or the customer(s) may be lost.

Based on declarations from XO senior personnel[5] and an Economist's Report[6] analyzing the FCC's Mandatory Data Collection, XO's comments on the *Special Access NPRM* provided evidence the ILECs have continuing market power, particularly in the provision of Dedicated Services channel terminations. In sum, XO's evidence showed:

- In all but the most dense central business districts ("CBDs"), there is limited in-building presence by multiple facilities-based competitors providing Dedicated Services.[7]
- In all but the most dense CBDs, there is limited potential competition from multiple facilities-based providers providing Dedicated Services. Moreover, even where competitive fiber networks may be near a building, there remain challenges or outright barriers to entry into that building because the network may be designed to provide only transport service, the costs to construct in the local environment may be high, there may be insufficient demand (which may be the result of the lock-up provisions discussed herein), local government may impose moratoria or other restrictions on construction, or building owners may not permit access.
- Where there are no competitors in-building, prices charged by ILECs are supracompetitive, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted]

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5 XO's *Special Access NPRM* Comments, Declaration of James Anderson ("Anderson SA Declaration"); Declaration of Michael Chambless ("Chambless SA Declaration"); and Declaration of George Kuzmanovski ("Kuzmanovski SA Declaration").

6 Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, WC Docket No. 05-25, RM-10593 (filed Jan. 27, 2016) ("Economist's SA Report").

7 The Economist's SA Report explains that the concerns with monopolies in Dedicated Services markets are at best only marginally ameliorated where there are duopolies. *See* Economist's SA Report ¶¶ 46-52.

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[redacted][8] **[END HIGHLY CONFIDENTIAL]**

- Rapid entry is difficult even in isolated cases and should not be expected in the near term on any scale to ameliorate the ILEC's market power as a general matter.[9]

As a result, XO called on the Commission to re-regulate the ILEC's provision of Dedicated Services by adopting and applying new triggers for pricing flexibility:

- <u>DSn Channel Terminations.</u> XO proposed that pricing flexibility for DSn channel terminations be granted within a CBD (or other contiguous, compact service area) when, in the aggregate, commercial buildings comprising more than 66% of the square footage of those buildings in the relevant area in which TDM services are offered have four or more competitors with in-building TDM facilities.[10]

- <u>Ethernet Channel Terminations.</u> XO proposed that pricing flexibility for Ethernet channels terminations be granted within a CBD (or other contiguous, compact service area) when, in the aggregate, commercial buildings comprising more than 66% of the square footage of those buildings in the relevant area in which fiber-based Ethernet services are offered have at least two or more competitors with in-building fiber facilities and at least two additional CLECs with fiber either in the same buildings or in close proximity to that location.[11]

- <u>Dedicated Services Transport.</u> XO proposed the Commission create density zones in an MSA and award relief when triggers are met within each zone. In particular, XO found that effective competition is predominantly present in Tier 1 cities within much of the CBD and the first ring of suburbs. These should comprise two separate areas for purposes of the transport trigger, and then outer rings around the CBD and first ring of suburbs should be defined for purposes of pricing flexibility.[12]

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8 XO's *Special Access NPRM* Comments at 51.

9 *Id.* at 46.

10 *Id.* at 44-55.

11 *Id.*

12 *Id.*

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Finally, XO proposed the Commission adopt interim pricing regulations where the triggers are not met to ensure that prices for Dedicated Services are just and reasonable where adequate competition is not present to eradicate ILEC market power.

B. <u>To provide retail commercial customers with choices for Dedicated Services prior to the development of facilities-based competition, it is important to have a robust wholesale market for copper loops and DSn circuits, which enable the provision of retail DSn and lower speed Ethernet services</u>.

XO prefers providing Dedicated Services over its network for many reasons: more rapid provision of services, greater ability to innovate, higher network reliability and quicker repair, and better margins. As a result and as discussed above, it has accelerated its investment in network facilities, including through its $500 million "On-Net Initiative" launched in 2014.[13] But, XO's on-net reach, even with this significant construction initiative, will still be limited to fewer than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted][14] **[END HIGHLY CONFIDENTIAL]** buildings in total.[15] In any one of the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Metro areas in which XO has

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13 Kuzmanovski SA Declaration ¶ 7. While XO can expand its network materially with $500 million of capital, it is still a small amount in comparison to the amount required to fully deploy to all buildings in even one Metropolitan Statistical Area ("MSA").

14 Declaration of Michael Chambless ¶ 5 ("Chambless Tariff Investigation Declaration"), submitted with these comments.

15 XO's decisions to build additional network facilities are targeted toward and triggered by immediate service opportunities. Moreover, XO's main focus is to build where it can leverage its network assets to reach additional customer locations– potentially a few thousand additional buildings – with "on-net" services to meet their present demand. Kuzmanovski SA Declaration ¶ 7; Anderson SA Declaration ¶ 5.

Metro fiber rings today, XO access only a very limited number of commercial buildings with lateral facilities. For example, XO has lit fiber only to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[16] Moreover, commercial customers often have multiple sites, many of which are outside CBDs, and serving these types of builds with on-net facilities is economically challenging in almost all cases, at best.

While XO is engaged in building facilities, it accesses facilities and services at wholesale from other network operators to provide retail customers with Dedicated Services.

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[16] *Id.* ¶ 14. The buildings where XO has lit fiber in these cities represent less than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** commercially available buildings in each city.

As for the overall presence of competitive facilities, the special access data collection demonstrated that in a clear majority of commercial buildings within central business districts, the ILEC is the only facilities-based provider, and the ILECs, nationwide, account for **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Measured either way, almost all buildings **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** have no more than two providers. When there is only one in-building provider, moreover, it is nearly always the ILEC. **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Economist's SA Report ¶ 44-45.

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Unfortunately, because competitive wholesale options are so limited, XO most often must turn to the ILECs.[17] This is especially true for copper loops and Dedicated Services channel terminations (DSn and Ethernet services), which for XO are used for a significant percentage of its retail sales of Dedicated Services and are expected to be used for many years.[18]

C. <u>By reducing wholesale access to ILEC Dedicated Services and to copper UNEs, the Commission effectively placed CLECs at the mercy of the ILECs to obtain wholesale access to Dedicated Services</u>.

The Communications Act of 1934, as amended,[19] gives the Commission substantial authority to enable CLECs to access ILEC facilities and services on a wholesale basis at rates, terms, and conditions which would foster competition while they build their networks. Unfortunately, the Commission has adopted a series of orders limiting CLEC access to ILEC facilities and services at regulated rates, terms, and conditions under the mistaken notion that

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17 This is evidenced by the data supplied to the Commission in the *Special Access NPRM*, which shows that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** most of which are concentrated in select, dense areas of MSAs. *See* XO's *Special Access NPRM* Comments at 32. XO finds that nearby providers will respond to a solicitation approximately **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the time when they are located near the building in question, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** feet depending upon the size of the expected spend. Chambless SA Declaration ¶¶26-27. For this reason, XO generally will consider soliciting bids from nearby competitors when they are within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** feet. *Id*. ¶ 26. Even where multiple competitors are present in-building, XO finds that ILECs generally have not lowered their wholesale prices in response.

18 *See* XO's *Special Access NPRM* Comments at 54; *see also* Section II.B *infra.*

19 47 U.S.C. § 151 *et seq.* (the "Communications Act").

robust facilities-based competition was well underway or would develop rapidly and pervasively. First, the Commission, using predictive judgment, permitted the ILECs to obtain regulatory pricing flexibility or "price flex" relief in the provision of DS1 and DS3 CBDs based on flawed competitive triggers.[20] Then in the *Triennial Review Orders*, it limited competitors' ability to access unbundled network elements ("UNEs") at regulated rates, terms, and conditions.[21] Additionally, the Commission effectively eliminated regulation of Ethernet services provided by ILECs.[22] These combined actions, all based on flawed premises, undermined the environment to foster the development of competition and had major negative consequences in the marketplace. The ILECs took full advantage of these deregulatory actions to maintain and extend their market power, including, as discussed extensively herein, by leveraging the "price flex" relief they

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[20] *See Access Charge Reform et al.*, CC Docket No. 96-262 *et al.*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd. 14221, 14257-307, ¶¶ 67-168 (1999).

[21] *See Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers et al.*, CC Docket No. 01-338 *et al.*, Report and Order on Remand and Further Notice of Proposed Rulemaking, 18 FCC Rcd. 16978, 17102-236, ¶¶ 197-416 (2003); *Unbundled Access to Network Elements et al.*, WC Docket No. 04-313 et al., Order on Remand, 20 FCC Rcd. 2533, 2558-96, ¶¶ 43-106 (2005) (collectively the "Triennial Review Orders").

[22] *See, e.g.*, Verizon Telephone Companies' Petition for Forbearance from Title II and *Computer Inquiry* Rules with Respect to their Broadband Services Is Granted by Operation of Law, WC Docket No. 04-440, News Release (rel. Mar. 20, 2006); *see also e.g.*, *Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to its Broadband Services; Petition of BellSouth Corporation for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to its Broadband Services*, WC Docket No. 06-125, Memorandum Opinion and Order, 22 FCC Rcd 18705 (2007).

received to impose lock-up requirements on CLECs seeking to purchase their wholesale DSn inputs to provide Dedicated Services at rates that were more reasonable than the ILECs' month-to-month rates, which remained supra-competitive.

In the *Suspension Order*, well over a decade after the "price flex" rules were adopted and many years after the ILECs had received relief in most major metropolitan areas, the Commission finally admitted that its pricing flexibility triggers "are not working as predicted"[23] and questioned its prediction that "collocators would eventually build their own channel terminations to end users."[24] Yet, the damage to competition has been done, and to undo it, the Commission will need to take steps to counter the continuing market power of the ILECs in most commercial buildings. In this tariff investigation, the Commission should act to end ILEC lock-up and related terms and conditions. In response to the *Special Access NPRM* as supported by the *Special Access Data Collection*, the Commission should re-regulate pricing of ILEC Dedicated Services.

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[23] *See Special Access for Price Cap Local Exchange Carriers,* WC Docket No. 05-25, *AT&T Corporation Petition for Rulemaking Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services,* RM-10593, Report and Order, FCC 12-92, 27 FCC Rcd 10557, ¶ 1 (rel. Aug 22, 2012) ("Suspension Order").

[24] *See id.*, ¶ 68.

II. XO'S SPECIFIC RELIANCE ON ACCESS TO WHOLESALE INPUTS FROM INCUMBENTS, INCLUDING DSN CIRCUITS

A. XO relies extensively on ILEC TDM DSn circuits as wholesale inputs to provide TDM and Ethernet services.

XO has metropolitan area fiber-based networks in many large and mid-sized metro areas over which it provides a variety of retail services to small and medium to large business and enterprise customers and Dedicated Services at wholesale to carrier customers.[25] XO metro and last mile fiber connects to more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** buildings over which XO provides "on-net" (Type I) services to thousands of customers.[26] XO provides service to many more end users and carriers using facilities and services it leases and purchases ("Type II" facilities or "off-net" services), in combination with XO's own metro network facilities or on a standalone basis.[27]

XO offers TDM phone and TDM DSn services to retail commercial customers and carriers. XO's provision of these services relies extensively on ILEC-provided loop or channel termination inputs, either UNEs or Dedicated Services.[28] **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of TDM DS1 and DS3 circuits, respectively, that XO obtains on a wholesale basis are provisioned by an ILEC

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[25] Kuzmanovski SA Declaration ¶ 4.

[26] *Id*.

[27] *Id*.

[28] Anderson SA Declaration ¶ 5; Chambless SA Declaration ¶ 18.

network.[29] While XO obtains some TDM special access circuits from other competitors, the competitors are mostly reselling the ILEC DS1 or DS3 circuits, as XO itself does.[30] Moreover, competitors today are not building TDM network facilities and near-net facilities-based providers are therefore not likely to assert any competitive pressure on ILEC DSn pricing.[31] XO also uses TDM wholesale inputs from ILECs to provision Ethernet services to retail commercial customers.[32]

In sum, XO makes, and has no choice but to make, substantial purchases of DSN services from the ILECs if it is to provide TDM and Ethernet services to the locations where customers require connections. Because the options to purchase from competitors are limited, XO has no choice but to obtain the best rates that it can from the incumbent. As discussed below, to purchase DSn services at rates that permit it to offer a competitive retail product, XO must consider the Discount Plans of the ILECs that are under investigation.

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[29] Anderson SA Declaration ¶ 5. (Mr. Anderson's declaration included a typographical error; the DS3 number should have been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** as reflected in the referenced Highly Confidential Exhibit B.) Virtually all dark copper loops used by XO for EoC service are provisioned by ILECs. Chambless SA Declaration ¶ 18.

[30] Anderson SA Declaration ¶ 5.

[31] XO's *Special Access NPRM* Comments at 53.

[32] Anderson SA Declaration ¶ 5.

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B. Despite the increasing importance of Ethernet in the Dedicated Services marketplace, XO's commercial customers continue to demand DSn Dedicated Services.

In their Direct Cases, AT&T and Verizon claim that the importance of tariffed DSn services is small and dwindling fast, such that the Commission need not devote attention to their special access lock-up agreements in this investigation. These claims, however, are refuted by the facts. Although XO receives **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[33] the volume of new TDM services, as well as installed TDM services, remains substantial. XO built its business on providing DS1 and DS3 TDM services, and XO's experience is that many of these TDM customers continue to value the service, often because they can use and derive maximum value from their legacy equipment.[34] In addition, many legacy TDM small to medium-sized business customers find TDM-based service to be sufficient for their needs. XO has found customers' attachment to TDM holds true even though Ethernet prices are dropping and performance is increasing.[35]

Moreover, when one looks at the trends of XO's installed base of DS1 and DS3 services, as well as new orders, it is evident that claims by AT&T and Verizon, the two ILECs whose Discount Plans under the investigation that are most problematic for XO, that DSn special access is no longer an important wholesale input are exaggerated. DSn special access will remain

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[33] XO's *Special Access NPRM* Comments at 17.

[34] Chambless SA Declaration ¶ 32; Anderson Declaration ¶ 5.

[35] Chambless SA Declaration ¶ 32.

important to competitive providers for many years. As Michael Chambless, XO's Vice President of Access Management and Planning, explains, as of year-end 2015, XO had almost **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** ILEC-provided special access DS1 channel terminations in place pursuant to the tariffs are under investigation. XO has over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS3 ILEC-provided channel terminations as well.[36] Further, although there has been a decline over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in the absolute numbers of special access DS1s and DS3s channel terminations, the decline is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** to suggest that DS1s and DS3s will not be used in substantial numbers for many years yet. For example, XO's DS1s purchased under its CDP with Verizon North declined from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** a decline of only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Similarly, the decline of DS1s in place in Verizon South is only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Declines in the Bellsouth region are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted]

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36 Chambless Tariff Investigation Declaration ¶ 8.

[redacted][37] **[END HIGHLY CONFIDENTIAL]** In the PacBell region, where XO had **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS1s installed as of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the decrease was **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Based on XO's internal projections, it anticipates approximately a net **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in its requirements for new and installed DS1 circuits nationwide in 2016.

Further, the declining numbers of DS1 circuits in particular, and DSn circuits overall, purchased by CLECs in any event is not evidence that demand is not locked-in in an unreasonable manner, as AT&T claims.[38] Rather, the change in demand indicates only that the retail market is moving away from DS1s – not that the levels of demand for DS1s have become

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37 Chambless Tariff Investigation Declaration ¶ 8. As noted above, the decline in DS3s is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** In the Verizon North and South regions, where **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS3s under the Discount Plans being investigated are located, the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Yet, even these rates of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** mean that DS3s will remain important for several more years. Chambless Tariff Investigation Declaration ¶ 9. More importantly, as discussed later, these rates of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** mean that XO will face shortfall penalties for DS3 circuits with **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** over the course of its CDPs entered into for DS1 and DS3 services in Verizon North and South regions in October 2014.

38 AT&T Direct Case at 10.

insubstantial. That fact underscores the onerousness of ILEC Discount Plans with minimum commitments that lock-up that demand. Accordingly, the Bureau should complete the investigation into the reasonableness of the terms and conditions of ILEC special access tariffed Discount Plans identified in the *Designation Order* expeditiously before any additional harm is done.

III. ILEC RACK RATES ARE TOO HIGH TO PERMIT COMPETITION BASED ON TYPE II INPUTS, MAKING UTILIZATION OF ILEC DISCOUNT PLANS NECESSARY.

A. <u>ILEC month-to-month rates for DSn SPA services would not allow XO to compete</u>.

While Verizon and AT&T assert that their month-to-month rack rates are reasonable because they have not been designated for investigation, as explained herein, the ILEC monthly rack rates for DSn are so artificially high as to renders unthinkable a business plan using DSn services purchased at those rates as a wholesale input. The wholesale prices charged by ILECs on a month-to-month basis under their tariffs which contain their Commitment Plans make clear that ILECs have not been constrained by competition in the Dedicated Services marketplace for DS1 and DS3 TDM circuits.[39] Under these plans, ILECs offer discounts of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** below their monthly tariff charges if a wholesale customer commits not to buy an absolute volume of services.[40] Thus,

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[39] XO's *Special Access NPRM* Comments at 34.

[40] In the case of Verizon, for example, if XO did not enter into a successor Commitment Discount Plan in 2014, XO faced an increase in monthly rates for DS1 and DS3 services of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** if it reverted to month-to-month rates. Chambless SA Declaration ¶ 39.

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cost savings are conferred not on production as a matter of scale, but simply on the basis of the wholesale customer committing to a percentage of historic purchases or purchases as of day one of the agreement, no matter how large or small. This alone demonstrates that the month-to-month tariffed special access prices reflect the ILEC's market power.

To get a reasonable discount from the ILEC month-to-month rates and offer services on a Type II basis in competition with the ILEC's retail services,[41] XO enters into multi-year volume and term commitments under the ILECs' tariffs by which it commits to purchase certain levels of channel terminations at a DS1 or DS3 level. Many of those plans are under investigation (the "Discount Plans"): XO is a customer of Verizon's Commitment Discount Plans for DS1 and DS3 services in both Verizon North and South territory, for example, under Verizon's FCC Tariffs Nos. 1 and 11. XO is also a customer under each of the four AT&T Discount Plans for DS1 services that are under investigation.[42]

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[41] At most, the ILECS' month-to-month rates may be tolerable for short term transition purposes, but were XO to pay the month-to-month rates for all or even a significant minority of circuits, it would not be able to compete. In reality, XO **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** uses the ILEC month-to-month rates of the ILECs, especially AT&T and Verizon.

[42] Chambless Tariff Investigation Declaration ¶ 6. *See Designation Order*, Appendix. XO is also a customer under the Verizon West Discount Plans being investigated (Verizon FCC Tariffs No. 14), the Frontier Plans in former Verizon West territories (Frontier FCC Tariff No. 5). Chambless Tariff Investigation Declaration ¶ 6. With one exception, XO does not take issue with the Verizon West, Frontier, and CenturyLink Discount Plans under investigation. The DS3 shortfall penalties for Verizon West and Frontier are based on full expectation damages, as discussed below, in contrast with their penalties for DS1 circuits, which are only a fraction of that measure. The DS3 shortfall penalties of these two carriers are unjust and unreasonable. In addition, as explained below, the tariffed plans of Verizon West and Frontier and the contract tariff of CenturyLink

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Even with these discounts, the ILEC rates for DS1 and DS3 special access are considerably higher compared to facilities-based rates offered by competitors where available. Mr. Chambless, in his attached Declaration reviews rates for representative competitive carriers able to provide DS1s and DS3s in several key Metro areas for XO in the Verizon North and South territories **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** and AT&T regions **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. As Mr. Chambless notes, the rate comparison shows that the average competitors' rates in the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon cities (in buildings where the competitors have facilities) are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** below the rates of the ILEC for zero-mileage channel terminations. In the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** AT&T cities, average competitors' rates are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** below AT&T's zero mileage rates.[43] When mileage charges are added for channel terminations that end in a remote central office, the difference becomes even more extreme because Verizon and AT&T

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underscore the unreasonableness of the Verizon North and South CDPs and the four AT&T Plans under investigation. *See* Section VII, *infra*.

43 Chambless Tariff Investigation Declaration ¶ 10. The comparisons show comparable differentials between competitors and ILEC rates in the Verizon cities for both DS1 and DS3 circuits. *Id.*

assess mileage charges but the CLECs do not. Specifically, where there is five miles of mileage charges, the competitors' rates in the Verizon cities are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** lower than Verizon's and, in the AT&T cities, are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** lower than AT&T's.[44]

Because the price differentials are so great, XO would, if it could, use alternative competitive provider pricing whenever possible. However, to meet its minimum commitments and avoid shortfall penalties, XO most often has no choice but to purchase special access from the ILEC under the Discount Plans, not only where the ILEC is the only provider in the building, but also when there are alternative providers. These irrational commercial actions, which are the result of the Discount Plans' percentage minimum commitments and shortfall penalties, are actions that XO would not take in a functioning market. If it were to do otherwise, XO's costs of service would increase unacceptably because, to avoid the shortfall penalties, XO would still have to purchase the ILEC DSn circuit over and above paying for the circuit from the competitive provider.[45] The net result is that competitively offered options, even if facially less costly, are nonetheless commercially unattractive. This tends to further lock-up demand and slows the development of competition. Indeed, as Mr. Chambless explains, because reduced purchases under the Discount Plans combined with declining demand accelerates the potential

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[44] Chambless Tariff Investigation Declaration ¶ 10.

[45] Chambless Tariff Investigation Declaration ¶ 11.

for imposition of shortfall penalties (i.e., significantly increased costs), **[BEGIN HIGHLY CONFIDENTIAL]** [redacted][46] **[END HIGHLY CONFIDENTIAL]**

B. <u>XO's entry into the ILEC SPA Discount Plans is not voluntary in any normal sense of the word</u>.

In light of the circumstances discussed above, XO has no choice but to enter into the Discount Plans of the ILECs under investigation. As noted earlier, due to the limited availability of competitive options and the lock-up provisions of the Discount Plans, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of XO's off-net purchases of DS1 and DS3 services, respectively, are obtained from the ILECs.[47] Given the high rack rates and the chilling effect they have on competition, contrary to Verizon's and AT&T's claims, XO does not freely enter into the ILEC Discount Plans. Rather, XO's entry into the plans is its only option to provide services to XO's customers and by reasonably competitive.

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46 Chambless Tariff Investigation Declaration ¶ 12.

47 *See* Anderson SA Declaration ¶ 5. (Mr. Anderson's declaration included a typographical error; the DS3 number should have been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** as reflected in his referenced Highly Confidential Exhibit B.)

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IV. XO HAS NO EFFECTIVE CHOICE TODAY AS TO HOW MANY CIRCUITS IT COMMITS UNDER THE VERIZON AND AT&T ILEC DISCOUNT PLANS

A. A high percentage of XO's Type II DSN SPA purchases today come from AT&T and Verizon (North and South).

XO's primary suppliers of DS1 and DS3 off-net wholesale inputs are AT&T, Verizon, and CenturyLink. For instance, approximately **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of active DS1s circuits at year end 2015 were obtained from AT&T and Verizon, respectively.[48] Another **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** were obtained from CenturyLink, with almost all of the remainder from competitive providers. Thus, because the terms and conditions under which XO purchases its DS1 circuits from Verizon and AT&T are so important, XO will focus its attention on those plans.[49]

Regarding DS3s, XO purchases almost **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of its off-net circuits from the ILECs.[50] However, of those DS3 circuits that it purchases under ILEC Discount plans, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** are purchased from Verizon.[51] Therefore, regarding DS3 special access, XO will focus attention in these comments only on the DS3 plans of Verizon.

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48 *See* Anderson SA Declaration ¶ 16, Highly Confidential Exhibit B.

49 XO does not take its DS1 and DS3 circuits from the CenturyLink Discount Plan under investigation.

50 *Id.*

51 Chambless Tariff Investigation Declaration ¶ 6.

B. When XO renewed its plans with Verizon and AT&T most recently, its ability to reduce its minimum commitments were non-existent to limited.

Both Verizon and AT&T claim in their Direct Cases that carriers choosing Discount Plans retain a considerable degree of control over the size of their minimum commitments. Verizon asserts that a carrier that has committed to a CDP has control over its commitment level "because it can reduce its total purchases from Verizon before entering into the CDP or NDP. And once that initial, customer-chosen commitment period expires, the customer can revise its commitment level before entering into a new CDP or NDP, depending on its needs at that time. Thus, assuming the customer planned ahead, it may use Verizon's special access services for an initial period and migrate to competitive suppliers when that initial period expires."[52] AT&T makes a similar statement, asserting that "[m]oreover, when the plans expire, customers are free to reset their commitment at whatever level they choose (if they choose to renew at all), as percentage commitments are not tied to historical purchases, but rather to purchases the customer chooses to bring within the plan in each contract period."[53]

However, in XO's experience, there is limited or no opportunity for a carrier to dictate what its minimum commitment will be. This is a result of the difficulties carriers like XO face in transferring circuits to other providers in a timely fashion without facing considerable shortfall penalties, assuming such options are even available.[54] As explained above, ILECs alone have near ubiquitous reach to commercial buildings giving competitors like XO limited options to

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52 Verizon Direct Case at 9.

53 AT&T Direct Case at 4.

54 Chambless Tariff Investigation Declaration ¶ 13.

transfer circuits to other providers, even if they are willing to face the shortfall penalties for the periods prior to renewals. XO details below the difficulties it has faced to "control" its minimum commitment without incurring huge shortfall penalties. At bottom, Verizon and AT&T claim that XO can either reduce its commitment levels before the contract period ends, incurring substantial shortfall penalties, or enter into a new commitment level at a higher level but with increased risk that it will incur shortfall penalties in the future. This is a Hobson's choice which highlights the unreasonableness of the terms and conditions of the Discount Plans of these two carriers.

1. *Verizon North and South*

XO did not have success reducing its commitment levels before the renewal of new agreements with Verizon recently, except involuntarily as the result of falling demand for DS1 and DS3 services. The Verizon CDPs in the old NYNEX and Bell Atlantic territories, i.e., Verizon North and South, respectively, require a carrier entering into the CDP to accept a minimum commitment of 90% of the in-service channel terminations as of the date of renewal.[55] Despite XO's attempts to lower its commitment level with Verizon, XO's CDP with Verizon as automatically renewed in 2014 based on previous commitment levels, locking XO into a commitment level of 90% of XO's inventory as of September 30, 2014.[56] **[BEGIN HIGHLY CONFIDENTIAL]** [redacted]

55 *See* Verizon Tariff FCC No. 1, Section 25.1.3 and Verizon Tariff FCC No. 11, Section 25.1.3.

56 Chambless Tariff Investigation Declaration ¶ 15.

[redacted] **[END HIGHLY CONFIDENTIAL]** Verizon CDP's in those regions required XO to purchase all DSn services under the CDP. Therefore, XO could not, for example, to address concerns about anticipated falling demand, replace special access circuits with UNEs at the end of its CDP term to lower the minimum commitment upon renewal.[57] XO looked into moving circuits to other providers through assumption agreements or grooms, but it did not prove practical to do this before renewal, in part because of general lack of ability to reduce its commitment and the increased potential for shortfall penalties resulting from moving customers off underlying circuits purchased under the Discount Plans as DSn demand continues to decline.[58] XO's new minimum commitments were lower than they had been under the expiring agreement, particularly in the case of DS3s, but this was a result of falling DS3 demand. In XO's experience, assumption agreements take approximately **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** from start to finish. Had XO opted to disconnect circuits before the end of the prior agreements, it would have resulted in more substantial shortfall penalties than those it suffered because of changing market conditions. Indeed, XO was assessed over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in shortfall penalties under its Verizon North and South CDPs between January 2013 and June 2014.[59] An

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57 *Id.*

58 *Id.*

59 *Id.* ¶ 16.

additional **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in penalties was assessed for the three-month period of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[60]

Significantly, at the time of renewal, Verizon required XO to purchase all DSn services under the CDP, preventing XO from converting any DS1s or DS3s to UNEs where they might have otherwise been available. Nor could XO move some of the circuits to month-to-month rates as it attempted to transition services to competitive providers or its own facilities (assuming they were available or it were economical to construct them), or even to a circuit-based term plan. In short, XO's DSn services were locked up with Verizon unless it was willing to face

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[60] *Id.* The shortfall penalty that Verizon sought to assess for the final three months of the previous DS3 CDP terms was found unlawful by the U.S. District Court for the Eastern District of Virginia because shortfall payments over three months are not provided for in the Verizon tariffs. *Verizon Virginia LLC v. XO Communications,* Civil Action No. 3:15-cv-171 (E.D. Va. Nov. 5, 2015), *appeal pending, Verizon Virginia, LLC v. XO Communications, LLC*, Case No. 15-2496 (4th Cir.).Nonetheless, despite the fact that the shortfall for July through September 2014 was found unlawful under the tariff, the size of the penalties Verizon sought to assess for this short period highlights what awaits a CDP customer that seeks to control its new minimum commitment by reducing its spend in the last period before renewal. The District Court also upheld Verizon's interpretation of its tariff in assessing the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in penalties, but did not make any findings regarding the Section 201(b) reasonableness of Verizon's tariff, which the parties agreed would not be decided by the court. XO appealed the court's interpretation of the tariff, arguing that there is a conflict and ambiguity within its terms that should be resolved in favor of an "expectation damages" measure of shortfall penalties based on what XO would have spent had it met its minimum commitment to purchase channel terminations. Verizon cross-appealed, challenging the court's rejection of Verizon's attempt to apply its tariff to assess a shortfall over a three-month, rather than a six-month period. The appeals are pending.

even more substantial shortfall penalties, which XO explains in Section IV are manifestly unjust and unreasonable.

2. *AT&T*

XO has had better, but still limited, success with reducing its commitment level under the AT&T Discount Plans when they were renewed in the past few years. Typically, XO's DS1 Discount Plans in three of the four AT&T regions – the old Ameritech, BellSouth, PacBell, and SWBT Regional Bell Operating Company territories -- have **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** terms. (XO's plan with Bell South is for **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[61] XO has enjoyed some **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in the AT&T regions converting DS1 special access circuits under the Discount Plans to UNEs, and it has the theoretical ability, at least, to move them back subsequently to special access to try to stay above the percentage minimum commitment and avoid shortfall penalties.[62] However, at some point, as demand for DS1s

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[61] Chambless Tariff Investigation Declaration ¶ 17. *See also* AT&T Tariff FCC No. 2, Section 7.4.13(A) and Section 7.4.18(A); AT&T Tariff FCC No. 73, Section 7.2.22(A).

[62] Chambless Tariff Investigation Declaration ¶ 17. *See also* AT&T Tariff FCC No. 1, Section 2.4.8. Whether UNEs at the DS1 level are available depends upon the presence of appropriate ILEC facilities – copper DS1 facilities are much easier to access and utilize as UNEs than fiber DS1 facilities – as well as whether the Commission's impairment triggers eliminating the ILECs' obligation to unbundle DSn circuits as UNEs in specific wire centers have been satisfied. As ILECs continue to retire more copper facilities, the availability of DS1 UNEs will become more problematic and tend to push competitors to greater reliance on DS1s Discount Plans to be able to compete using ILEC wholesale inputs.

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continues to slide, any UNEs XO has "in reserve" to convert will be exhausted, and XO will face shortfall penalties, which, as explained in a later section, are largely unjust and unreasonable.

As Mr. Chambless explains, XO entered into a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS1 commitment with Ameritech under a Discount Commitment Program ("DCP") Plan starting in October 2015. Unlike Verizon, Ameritech allowed XO to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** which effectively, at the time of Plan renewal, removed them from the percentage minimum commitment level. However, XO's ability to move the circuits has been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. After identifying **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**, Ameritech and XO are still working to convert the identified circuits **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** The delays in the full conversion arise for a variety of reasons, some attributable to both parties, including limitations on the daily pace of conversions permitted by the ILEC. This long conversion period highlights the difficulties of moving circuits serving customers out from under Discount Plans in a timely fashion so to avoid shortfall penalties by

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starting too early or getting locked in at an unreasonably high minimum commitment at the time of transition if not completed.[63]

XO renewed its **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Discount Plan agreements with AT&T in March 2015 in the Southwestern Bell and PacBell regions.[64] Prior to the renewal, as Mr. Chambless explains, XO converted **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of its DS1 special access circuits to UNEs. XO is closely monitoring the numbers of DS1s that remain active under the Plans on a month-to-month basis to manage its commitment level under that agreement. As explained below, the DS1 shortfall penalties under the Discount Plans being investigated in the Southwestern Bell and PacBell territories are outrageously high.

V. THE MINIMUM COMMITMENT LEVELS ARE UNJUST AND UNREASONABLE

The minimum commitment provisions of the ILECs, in particular the CDPs Verizon North and South and the four AT&T Discount Plans under investigation, operate to lock-up the demand of wholesale customers. Significantly, as detailed in this section, neither Verizon nor AT&T are able to offer any rational justification for these minimum commitment provisions.

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63 Chambless Tariff Investigation Declaration ¶ 18. As Mr. Chambless explains in his Declaration, in the case of Ameritech, the ILEC has been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** This is the only time that an ILEC has extended such an accommodation. *Id.*

64 Chambless Tariff Investigation Declaration ¶ 19.

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Neither party claims, for example, that minimum commitment levels are tied to economies of scale and the size of the discounts, which would be difficult since the discounts are not tied to circuit volumes, as both ILECs freely admit.[65] Consequently, the Commission should, in the absence of any countervailing reasons to offset the serious and adverse consequences of the minimum commitment provisions, find them unjust and unreasonable and require the ILECs to eliminate them and replace them with provisions that satisfy Section 201(b) of the Act.

A. <u>Verizon's Minimum Commitment Levels Are Unjust and Unreasonable</u>.

Verizon's Direct Case acknowledges that its minimum commitment provisions were not supported by any cost-justification prepared by the ILEC.[66] Indeed, Verizon admits that it is "[un]aware of existing documents that would demonstrate the methodology and calculations used to determine the percentage thresholds."[67] This leaves Verizon scrambling after the fact to look for justifications, but it is unable to find any that satisfy or would countenance the adverse consequences documented above.

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65 AT&T Direct Case at 4. AT&T's description of its Plans as early termination liability avoidance plans provides no assistance in understanding the minimum commitment percentages. *Id.* at 16-19.

66 Verizon Direct Case at 48.

67 Verizon Direct Case at 89. To remove any doubt on this score, Verizon adds that it "designed the CDP almost 20 years ago, and we are not aware of current documents that can explain specific methodologies or calculations used to determine the percentage thresholds in the CDP. Nor is Verizon aware of other thresholds that may have been considered for the CDP or NDP." *Id.*

While it may be that no cost justification was required as a regulatory matter when the Verizon CDPs were first tariffed, the lack of a cost justification undermines many of the claims that Verizon nonetheless proceeds to make. For example, Verizon asserts that the averaging of the commitment period was "designed to ensure that the customer has made a commitment sufficient to warrant the discounts provided."[68] However, in the absence of any cost justification, what basis does Verizon have to claim that the commitments are sufficient to warrant the discounts provided? Verizon's rationale is particularly lacking, given that the discounts are not based on actual volumes of channel terminations purchased, or the revenues paid therefore, but based on the commitment to purchase 90% of the in-service channel terminations at the time of renewal, whatever that actual number may prove to be. How can a discount of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** for DSn channel terminations[69] be warranted without regard to whether a customer's commitment is to purchase 10 circuits, 100 circuits, or 10,000 circuits?

In the end, Verizon resorts to claiming that "[i]n general, Verizon intended the percentage thresholds under its term-discount plans with portability to be customer-friendly."[70] Making the unremarkable observation that "a 100% commitment level would not have been well received by our customers," Verizon goes on, without further support, to aver that "Verizon established

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68 Verizon Direct Case at 32.

69 *See* Chambless SA Declaration at 32.

70 Verizon Direct Case at 89.

minimum commitment levels below 100%, to balance our customers' needs and Verizon's."[71] But such assertions carry little weight because they provide no insight into why a 90% minimum commitment balanced customers' needs either when adopted or, where demand for DS1 and DS3 special access is declining.[72] Not knowing the basis for why the CDP minimum commitment percentages were adopted in the first place makes it impossible to give any consideration to after-the-fact make-weight justifications as to why they are just and reasonable today. The Commission should reach no conclusion other than the percentage is arbitrarily high, and therefore unjust and unreasonable in violation of Section 201(b).

B. <u>AT&T's Minimum Commitment Levels Are Unjust and Unreasonable</u>.

AT&T tries to deflect scrutiny against the minimum commitment percentage in its Discount Plans by claiming that "the 'percentage commitments' are simply backstops that limit AT&T's exposure when customers want the flexibility to break their term plan commitments without the normal early termination liability ('ETL')."[73] This begs the fundamental question,

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[71] *Id.*

[72] The fact that, in the case of the DS1 Eight and Ten Year Term Volume Plan ("ETTVP"), Verizon arrived at the 90% figure applicable to that plan as the result of negotiations with AT&T, does not justify the use of that percentage with other competitors then or with any competitors today. Moreover, that negotiation with one carrier in connection with that plan is not a justification for the percentage used in the CDP plans from which XO purchases. Verizon's claim that it reached the minimum commitment percentage in the ETTVP via negotiation underscores the unreasonableness of giving competitors under its plans no choice in what the percentage will be or having an independent justification for why the percentage is what it is.

[73] AT&T Direct Case at 4.

however, of what the percentage should be. This AT&T never answers and, unlike Verizon, never even purports to answer why AT&T selected 80% of in-service channel terminations at inception as the minimum commitment level. AT&T's asserts that "[t]he minimum commitment levels are set low enough to give the customer plenty of flexibility to manage a natural level of churn in its base of circuits without incurring ETLs, but not so low as to upset the overall balance of AT&T's overall special access rate structure, which includes month-to-month, term only, and term plus portability plans."[74] But these claims simply are not supported by any facts or analysis and, in the end, the Commission is left to conclude, like the child listening to the story of *The Three Bears*, that the AT&T percentage commitments, like Baby Bear's porridge, are just right.[75]

AT&T attempts to explain away the lack of justification for the percentage commitments by arguing that "customers are free to reset their commitment at whatever level they choose (if they choose to renew at all), as percentage commitments are not tied to historical purchases, but rather to purchases the customer chooses to bring within the plan in each contract period."[76] However, absent the ability to materially alter the volume of circuits without potentially incurring shortfall penalties, AT&T's plan in this regard differs little from Verizon's, if for no other reason than alternative provider options are limited. In these circumstances, whether the

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[74] AT&T Direct Case at 19.

[75] A further measure about how the percentage minimum commitment provisions of AT&T and Verizon are unjust and unreasonable is that they both offer similar after the fact justifications for different percentages, Verizon's 90% and AT&T's 80%.

[76] *Id.; see also id.* at 17-18.

commitment is based on the number of circuits in place at the time the prior agreement expires and the new one takes effect or the percentage commitment is tied to what the customer chooses to bring within the plan in each contract period, the result is the same if there is inadequate choice and the demand for the circuits is falling quickly enough to more than likely ensure there will be shortfall penalties before the end of the agreements' terms.[77]

AT&T also tries to defend its minimum discount percentages by claiming that they give customers of the Discount plans adequate "headroom" to add or decrease the number of DS1 circuits and still get the discounts.[78] AT&T adds that "no CLEC with headroom **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** could possibly be forced to maintain unneeded facilities."[79] But the fact of the matter is that, as demand for DS1 declines, especially if that decline accelerates, there will be insufficient "headroom," and shortfall penalties will begin to apply. Thus, even to the extent that a wholesale customer can select a lower commitment, because the same 80% minimum commitment percentage will be in place, the decline in DS1 demand may lead to unreasonable shortfall penalties applying in any event. Thus, in those circumstances, the commitments will

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77 Certainly, wholesale customers cannot be expected to simply leave their existing customer base stranded.

78 *See. e.g.*, AT&T Direct Case at 4 ("These plans give them that flexibility, and most even enable them to disconnect a significant percentage of their circuits that are still under term commitments without replacing them or incurring ETLs."); *id.* at 19 ("The minimum commitment levels are set low enough to give the customer plenty of flexibility to manage a natural level of churn . . ..").

79 *Id.* at 45-46.

not be low enough to provide flexibility to manage a "natural" level of churn, a concept which remains ambiguous despite AT&T's claims.

In the end, AT&T fails like its counterpart Verizon to offer a feasible basis justifying the minimum commitment percentage in its Discount Plans. Thus, the AT&T Discount Plans provisions that require a minimum commitment based on a percentage of a customer's in service circuits – those that the customer presents at the Plans' inception – are unjust and unreasonable.

VI. MANY OF THE SHORTFALL PENALTIES IN THE DISCOUNT PLANS UNDER INVESTIGATION ARE UNJUST AND UNREASONABLE

In the Discount Plans under investigation, XO faces a variety of shortfall penalty provisions which apply should XO fail to meet its minimum commitments under the Plans to maintain a certain level of in-service DS1 or DS3 channel terminations. Because these penalties are calculated in such a myriad of ways, it is highly questionable whether any of them can be warranted. This is especially the case since the same justification is given for each – namely, to give the ILEC the "benefit of the bargain" if the minimum commitment is not satisfied.[80] As discussed in more detail below, taking this inconsistent set of shortfall penalty provisions together with current market conditions of declining demand and the objectionable percentage-based commitment requirements described above, the terms and conditions concerning these shortfall penalties are unjust and unreasonable in violation of Section 201(b).

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[80] Verizon Direct Case at 14, 27, 30, 35; AT&T Direct Case 19.

A. Certain of the ILEC's shortfall penalties are directly tied to full or partial "expectation damages."

Some of the ILEC shortfall penalties appear to be based on the premise that an ILEC offering a Discount Plan has a certain expectation of revenues directly tied to the minimum commitment made by the Discount Plan customer. The minimum commitments are tied to keeping a certain level of channel terminations active over a certain period of time, whether each month or on average over a period of months. When a customer falls short of the minimum commitment over the measurement period, the penalty is assessed, in effect, by multiplying the rate for the channel terminations times the size of the shortfall times the number of months in the measurement period. However, the penalties based on this "expectation damages" premise in the different plans are inconsistent, because some are based on full expectation damages while others are based on as little as 33% of expectation damages. The Direct Cases do not help explain why some Discount Plans that use an "expectation damages" measure for shortfall penalties are set at 100% and others find something less sufficient. This lack of explanation makes questionable the premise that there is a real "expectation" loss when a customer fails to meet its minimum commitment, especially when combined with the fact that the Plans' discounts are available to customers regardless of the size of their commitment. These inconsistencies and lack of justification exposes even the penalties based on mere expectation damages as unjust and unreasonable in violation of Section 201(b).

Examining some of the penalties based on "expectation damages" will illustrate the inconsistency and arbitrariness of the penalties. In XO's DS1 agreement with Bell South, XO receives a discount for a level of channel terminations to which it voluntarily commits (unlike the other AT&T regions). Charges for DS1s in the region under the Plan that exceed that amount are charged at a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[81] XO currently faces a penalty if it falls short of the commitment, but the penalty is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** per DS1 channel termination that makes up the shortfall, which is less than the channel termination price.[82]

In other AT&T regions, the penalty is more directly tied to expectation damages. In Ameritech region the measurement period is a given month ("Month One"), but Ameritech provides a grace period should the number of in-service DS1s be at or above the minimum commitment three months later ("Month Four").[83] If the customer fails to bring the number of "in active service" DS1s above the minimum in Month Four, then the penalty is assessed for Month One equal to the number of channel terminations that make up the shortfall times the monthly charge.[84] The reason for this cure period is not explained in AT&T's Direct Case, although given the overall trend of declining demand for DS1s and DS3s, it is increasingly

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81 Chambless Tariff Investigation Declaration ¶ 20. The BellSouth arrangement puts to the lie AT&T's claim that Discount Plan customers have a degree of "headroom" to increase or decrease their spend above or below the minimum commitment without incurring a penalty, at least in that region. *See* AT&T Direct Case at 21.

82 *Id.* ¶ 23.

83 *Id.* ¶ 22. *See* AT&T Tariff FCC No. 2, Section 7.4.13(C). In Ameritech, there are state-specific minimum commitments, in contrast with the region-wide minimum commitments in the other three AT&T regions. *Id.* *See* AT&T Tariff FCC No. 2, Section 7.4.13(A).

84 *Id.* *See also* AT&T Tariff FCC No. 2, Section 7.4.13.

unlikely that a customer would be able to make up a shortfall three months later. It is more likely the shortfall will have remained or even grown.

In several other ILEC regions, however, the penalty for a DS1 shortfall under a plan is less than the monthly rate. Specifically, in Frontier and Verizon West, the amount of shortfall, if any, is assessed over a twelve month period. However, the penalty is not twelve times the monthly rate times the number of average channel terminations the customer falls short, but only four times.[85] Thus, Verizon West and Frontier assess a much smaller expectation damages-based penalty for the same purpose as Ameritech, making any justification for the Ameritech penalties unreasonable in comparison.

B. <u>The per DS1 shortfall penalties in the Southwestern Bell and PacBell territories are higher than the monthly charges of a channel termination.</u>

In sharp contrast with the other AT&T regions, both Southwestern Bell and PacBell impose a shortfall penalty in the form of a "non-recurring charge" or NRC of $900 per DS1 channel termination for the number of channel terminations, if any, the Plan customer falls short of the minimum commitment.[86] This penalty, which is reassessed in the first month there is a shortfall, is several times the monthly charge for a channel termination. While the charge is labeled as non-recurring, unless XO is able to add a circuit to make up for the shortfall,

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[85] *Id.* ¶ 24; *See* Frontier Tariff No. 5, Section 5.6.14; Verizon Tariff FCC No. 14, Section 5.6.14. In the case of DS3 plans in Frontier and Verizon West, by contrast and inexplicably, the shortfall penalty is twelve times the monthly rate times the number of average channel terminations the customer falls short. *See* Frontier Tariff No. 5, Section 5.6.19(F); Verizon Tariff FCC No. 14, Section 5.6.19(F).

[86] *See, e.g.*, AT&T Tariff FCC No. 1, Section 31.5.2.7.1(A) and 7.4.18(E)(4).

additional penalties will recur in successive months at the rate of expectation damages.[87] While XO might be able to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** to make up for the shortfall in some instances, it often cannot do so. And if the shortfall is closed in the following months, the customer would face the same $900 per DS1 penalty if there is a subsequent shortfall. This shortfall penalty is patently unjust and unreasonable because it bears no relationship to the charge for a channel termination, and leads to an effective rate for any channel termination that the customer falls short that is well above the month-to-month rate. Such a penalty gives AT&T a potentially huge windfall if there is a failure to meet the minimum commitment, not the benefit of the bargain by any stretch of the imagination.

C. <u>Verizon North and South's shortfall penalties are overloaded and materially exceed any measure of expectation damages</u>.

Verizon's shortfall penalties have proven to be **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the cost of a channel termination and are therefore unjust and unreasonable on their face. XO has faced these penalties **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon's penalties as set forth in its Tariffs No. 1 and 11 and interpreted by Verizon do more than provide for expectations damages when the customer fails to meet its minimum commitment, which is based solely on channel terminations and measured over a six-month period. In Verizon's shortfall calculations, it

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87 Chambless Tariff Investigation Declaration ¶ 25.

calculates an average monthly rate for channel terminations to be applied to the shortfall below the minimum commitment, which is based on a channel termination spend. However, rather than using the charges for channel terminations to calculate that average, Verizon sums the total monthly charges billed to XO associated with all rate element charges, including channel terminations, transport mileage, and multiplexing arrangements, for the given service type over the measurement period. As a result, even though the minimum commitment is based only on channel terminations, Verizon effectively assumes for every channel termination XO would have spent to make up the shortfall, it would have purchased additional mileage and multiplexing ("MUXing") along with the channel terminations to make up the shortfall. But there is no basis for this because MUXing is not associated with channel terminations, only with transport, as are most of the mileage charges assessed against XO. The overwhelming majority of channel terminations are not purchased with mileage. Thus, the average monthly channel termination rate that Verizon uses is "overloaded" with allocations from rate elements – MUXing and mileage – exclusively or principally associated, respectively, with unrelated transport purchases (and) not needed to meet the minimum commitment.[88]

For example, for the most recent measurement period under XO's DS3 CDPs from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon billed XO a total Shortfall Adjustment in its North and South regions of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY**

88 Chambless Tariff Investigation Declaration ¶ 26; *see also* Verizon Tariff FCC No. 1 § 25.1.7(B), ¶ 3; Verizon Tariff FCC No. 11 § 25.1.7(B), ¶ 3.

CONFIDENTIAL] based on its interpretation of its tariffed formula. However, that penalty is almost **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of an expectation damages measure of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** based on the zero-mileage channel termination rate times the average monthly shortfall.[89] For the periods **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon assessed total shortfall adjustments for DS3 services against XO totaling more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[90] This amount is more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the amount that Verizon could have expected to receive were XO to have met its minimum commitment.[91] Indeed, the effective rate Verizon charges for the channel terminations that make up the shortfall are well in excess of Verizon's month-to-month rates which are, for example **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** higher than the discounted rates for DS1, well below the percentage increase represented by the shortfall penalties.[92]

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89 *Id*. In Verizon South, which involved the larger share of the total penalty, the shortfall penalty is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the full measure of "expectation damages." *Id*.

90 *Id*.

91 *Id*.

92 *Id*.

Verizon's penalties under its DS1 and DS3 CDPs in its North and South regions are each based on the same tariff language and are grossly disproportionate to expectation damages. Moreover, Verizon's tariff language, as interpreted by Verizon, places no limit on how high the penalties may be given the same amount of shortfall in channel termination purchases, even though the minimum commitment is based on channel terminations alone.[93] Greater purchases of interoffice transport, for example, would make the penalties even higher. Thus, inexplicably, if XO increased Verizon's revenues by purchasing more interoffice transport (i.e., more mileage transport and multiplexing), but there was a shortfall in channel termination purchases, any shortfall penalty would be greater than if XO purchased less interoffice transport.[94] The fact that a CDP customer's shortfall penalties would go up the more it purchases from Verizon underscores the unreasonableness of Verizon's shortfall penalty structure.

Further, the number of transport circuits XO purchases of a given service type is wholly independent of the number of channel terminations it purchases. As Mr. Chambless explains, Verizon's "overloaded" penalties are unfair because the number of DS3 transport circuits XO

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93 Verizon's shortfall penalties, i.e., the average per channel termination rate that will be used to calculate the penalty, are unknowable in advance even if one knows the number of channel terminations the customer will fall short because the complex formula in effect is based in large part on data outside the tariff (the customer's actual purchases of mileage and MUXing unrelated to channel terminations). Thus, the Verizon shortfall penalties are not clear and explicit and the shortfall rate formula, as a practical matter, includes unlawful references to outside instruments in violation of the FCC's regulations. *See* 47 C.F.R. §§ 61.2(a) and 61.74.

94 XO has been working to move **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** even if in some cases the alternative may not be advantageous. Chambless Tariff Investigation Declaration ¶ 30.

purchases is independent of the number of DS3 channel terminations it purchases. XO uses those types of circuits for two different reasons – transport circuits for interoffice connects and channel terminations to connect XO equipment with end users, and does not combine them to serve the same customer. Historic data confirms the trends for these two categories of circuits are not coupled. Rather, when the number of DS3 transport circuits XO purchases change only a few percent from one period to another, the change in channel terminations is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** For example, in Verizon North, between **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the number of DS3 transport circuits fell only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** but the total number of channel terminations over that same period fell **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** The comparison in Verizon South is almost as dramatic, a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** decrease for DS3 transport relative to a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** decrease for DS3 channel terminations over the same period.

Moreover, more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the DS3 channel termination circuits XO purchased in the periods when there were shortfall penalties assessed in 2013 and 2014, for example, are standalone or zero-mileage circuits without any mileage charges. The high percentage of channel terms without

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mileage underscores the unfairness of basing the penalties above "expectation damages" predicated on zero mileage channel termination charges.[95]

Verizon claims that "shortfall payments assessed on customers have been small compared to the total purchases under these plans, equaling less than 3% of Verizon's revenue under VCDP and 1% of Verizon's revenue under NDP."[96] In XO's experience, the shortfall penalty are typically **BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** or more of the revenues in Verizon territory based on the shortfall penalties that have been applied to it. For example, in the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon assessed DS1 and DS3 shortfall penalties of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** and the charges for the circuits actually purchased was **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** making the shortfall penalty over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the charges assessed for actual services.[97] When compared to the charges for channel terminations, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the shortfall penalty for missing the minimum commitment to purchase channel terminations was **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY**

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[95] Chambless Tariff Investigation Declaration ¶ 29; *see also id.* Exhibit C.

[96] Verizon Direct Case at 30.

[97] Chambless Tariff Investigation Declaration ¶ 31.

CONFIDENTIAL] of the amount XO paid for channel terminations in the same period.[98] In the earlier periods when Verizon assessed penalties, the size of the shortfall penalty was far more significant relative to the amounts paid for services than Verizon suggests. However, even if shortfall penalties account for a small percentage of total SPA revenues, this does not make them more just and reasonable. The issue is how large are the penalties compared to the amount of shortfalls below the minimum commitments. If the shortfall penalty exceeds what the contract price would have been had there been no shortfall, the penalty should be declared *per se* unjust and unreasonable.

D. Neither Verizon nor AT&T can justify the levels of their shortfall penalties.

In their Direct Cases, AT&T and Verizon acknowledge that they never submitted a tariff justification when proposing the tariff terms covering shortfall penalties. The ILECs argue that there are significant costs associated with portability.[99] However, they have not demonstrated how the amount of those costs or how they relate to the shortfall penalties they charge. Verizon acknowledges that no justification for the shortfall penalties has ever been provided to the

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98 *Id.*

99 Verizon claims that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** (Verizon Direct Case at 8). However, this number does not match XO's records, which show the number to be **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** under the commitment plans. In addition to overstating the number, Verizon does not demonstrate how that portability has actually resulted in increased costs. Chambless Tariff Investigation Declaration ¶ 32.

Commission.[100] AT&T and Verizon impose their unjustifiable shortfall penalties because they can, i.e., because of their unparalleled and unchallenged reach to commercial end user locations, they have the market power to do so.

Having failed to provide a cost study to justify their shortfall penalties, AT&T and Verizon argue that the shortfall penalties relate to the nature of the bargain.[101] As an initial matter, the ILEC tariffs are not the result of any bargain, and XO has not negotiated the tariffed rates. Even if this were an appropriate rationale, AT&T and Verizon's proposed analysis cannot apply here, where both AT&T and Verizon have different calculations for their shortfall penalties. Further, there is significant shortfall penalty variation within AT&T's four regions, as explained, and Verizon West imposes much different shortfall penalties than Verizon North and South. Moreover, XO has been forced to enter into Discount Plans to get a somewhat reasonable rate for DSn inputs because it lacks alternative competitive provider options in most locations. AT&T and Verizon's position is based on the premise that XO enters into the commitment plans by choice, but as demonstrated in XO's *Special Access NPRM* comments, that is not the case. If anything, the contract is one of adhesion.

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100 Verizon Direct Case at 48.

101 AT&T argues that "In exchange for bearing those increased risks and costs, the plans include potential shortfall liabilities, both to establish a reasonable outer boundary on the uncompensated costs AT&T will potentially bear, and to act as a contract enforcement mechanism with regard to the new, re-balanced bargain." AT&T Direct Case at 19. Verizon claims that "the shortfall provisions in the VCDP and NDP that enforce this commitment are not punitive. Rather, they ensure that Verizon receives the benefit of the bargain it struck with its customer." Verizon Direct Case at 30.

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E. <u>Regardless of form, the shortfall penalties imposed by Verizon and AT&T and unreasonable</u>.

Even where the shortfall penalty is more "reasonable," and based on an expectation standard, the shortfall penalties are unreasonable given the market and the overall structure of the commitment plans. Current market conditions with DS1s falling make long term commitments unreasonable, yet long term commitments are the only way that XO can obtain the price discount needed to compete in the marketplace. The inability to switch from TDM to Ethernet and have it count toward a minimum commitment further exacerbates the unfair lock-up and is in itself unreasonable. Ultimately, XO is put into a position of paying for service that it does not take, often because existing customers are migrating from DSn TDM services to Ethernet services and fewer new orders are coming in.[102] Where XO purchases the migrating customer's Ethernet service from the ILEC on a wholesale basis, and it fails to meet its DSn minimum commitment as a result, this means that XO, in effect, is paying for service for that customer twice.[103] This is especially unfair where the replacement service (*e.g.*, DS3 or Ethernet) is also purchased from the ILEC combined with fact that XO could not and cannot practically speaking lower its minimum commitment.

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102 As Mr. Anderson explains, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Anderson SA Declaration ¶30.

103 *See generally* Chambless SA Declaration ¶¶ 29-45.

VII. A COMPARISON OF OTHER ILEC PLANS HIGHLIGHTS THE UNLAWFULNESS OF THE VERIZON AND AT&T PLANS

XO has Dedicated Services agreements with numerous ILECs, enabling it to identify when incumbents are using their market power to exact unreasonable and unduly onerous requirements. In this section, it compares the terms and conditions in the Verizon and AT&T plans, particularly with regard to minimum commitments and shortfall penalties, those with those found in the plans of three other ILECs, Verizon West, Frontier and a contract tariff agreement offered by CenturyLink. As demonstrated below, this comparison makes more apparent the unjust and unreasonable nature of the terms and conditions in the Verizon and AT&T plans.

A. <u>The unreasonableness of AT&T and Verizon percentage minimum commitment requirements is underscored by the freedom of choice other ILECs offer wholesale customers.</u>

A key distinction between the Verizon and AT&T plans and those of other ILECs is the minimum commitment requirement. As previously explained, Verizon and AT&T require wholesale customers, when renewing, to commit to purchase an amount of TDM service inputs based on a high percentage of a customer's historical spend on these inputs. In contrast, Verizon West, while still imposing a minimum commitment requirement, allows wholesale customers to choose their purchase commitment levels that will fall under its Term Volume Plan without reference to historic spend.[104] The available discount escalates as a customer's commitment

[104] Verizon F.C.C. Tariff 14, Section 5.6.14(F) (For DS1s, "[w]hen the customer elects to enroll in a [one-, two-, three- or five-year DS1 term volume plan] the customer must specify, in writing, the enrollment date (which will be the anniversary date) and the DS1 SAL commitment quantity."). Verizon F.C.C. Tariff 14, Section 5.6.19(B)(1) (For DS3s, "A customer wishing to subscribe to a DS3 TVP must submit a written request to the

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increases.[105] Additionally, unlike the historic spend minimum commitments utilized by Verizon and AT&T, wholesale providers that purchase DS1s from Verizon West under its Term Volume Plan are permitted to increase or decrease their commitments throughout the term of the agreement without incurring a substantial penalty.[106]

Frontier offers a term and volume discount plan (F.C.C. Tariff No. 5) similar to that of Verizon West. Customers are permitted to select both the length (between one and ten years) and volume (between two and 11,000+ circuits).[107] As with Verizon West, Frontier's discounts increase as a customer's term and volume commitments rise.[108] While XO objects to any

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Telephone Company. The written request must be submitted in a manner designated by the Telephone Company, and must include all of the following. … (b) The DS3 Commitment Quantity for the DS3 TVP. … In order to subscribe to DS3 TVP, a minimum of twenty (20) DS3 SALs must be committed to the DS3 TVP.").

105 Verizon F.C.C. Tariff 14, Section 5.6.14(D) (For DS1s, "[r]ates are applied based on the following DS1 SAL threshold levels: 2-60, 61-120, 121-240, 241-500, 501-1000, 1001-3000, 3001-6000, 6001-11,000 and Over 11,000.").

106 Verizon F.C.C. Tariff 14, Section 5.6.14(G) (For DS1s, "[i]f the number of DS1 SALs increase from the initial commitment, the customer will have the option of increasing the commitment level for the remainder of their TVP. If the customer chooses not to increase the commitment level, he/she may covert the increased number of DS1 SALs to a monthly plan or a second TVP plan. The customer may decrease the commitment level at the time of the annual review and pay the applicable penalties for the amount of DS1 SALs being decreased.").

107 *See* Frontier F.C.C. Tariff No. 5, Section 5.6.14(A).

108 *See, e.g.*, Frontier F.C.C. Tariff No. 5, Section 5.7.18(A)(4). For instance, if a customer chooses to purchase DS1s in California from Frontier under a 5-year commitment, the monthly rate for a commitment between 1,001 to 3,000 circuits is $129.40 per DS1. The price would decrease to $127.31 per DS1 if the customer increased its commitment to 3,001 to 6,000 circuits.

minimum commitment requirement, it is less troubled by a plan that allows a wholesale customer to choose its commitment level than Verizon and AT&T's practice of imposing a level based on previous spend and with no regard to that customer's forward-looking demand for TDM services.

A contract tariff offered by CenturyLink also demonstrates the difference between reasonable terms and conditions and the unjust and unreasonable ones imposed Verizon's and AT&T's plans.[109] Under this contract, the purchaser discounts on purchases of certain services from CenturyLink if it meets certain spend levels, and the percentage of these discounts escalates as purchases increase. However, unlike the Verizon and AT&T plans, commitments to purchase in any given period and obligations to maintain those purchases are not required. Thus, if the purchaser spends between $2,000,000 and $2,699,999 to purchase qualifying services from CenturyLink, it will receive a 15.7% discount on the purchase price for those services.[110] This discount increases to 18.7% if the purchaser spends between $2,700,000 and $3,019,999 for any purchases that total more than $6,200,000, the purchaser can receive a maximum discount of 27.7%. Moreover, in calculating the discount based on the amount purchased, CenturyLink will include purchases for both DSn and Ethernet services, an approach that reflects the technology

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[109] *See* CenturyLink Operating Companies Tariff FCC No. 11, Section 24.2 (attached hereto).

[110] *Id.*

transition to fiber-based IP services not seen in the Verizon or AT&T Discount Plans.[111] In sum, the discounts available under the CenturyLink agreement are strictly volume-based and do not require the purchaser to commit to and maintain any minimum purchase level to receive them.

B. The unreasonableness of the shortfall penalties imposed Verizon and AT&T is plain when compared with the penalties of several other ILECs' plans.

As noted above, the Verizon North and South shortfall penalty calculation results in a windfall considerably above expectation damages. The Southwestern Bell and PacBell shortfall penalty provisions dictate an excessive penalty in the first month, several times the monthly DS1 rate, ensuring that shortfall penalties over an extended period will exceed expectation damages. The Ameritech DS1 shortfall penalties and the Verizon West and Frontier penalties for DS3 shortfall penalties are based on a full measure of expectation damages.

The DS1 shortfall penalty in the Verizon West Discount Plan is based solely on a limited percentage of expectation damages, which means that a wholesale customer will be liable only if it fails to maintain an adequate number of circuits in accordance with its self-imposed purchase commitment, and liability is limited to a fraction of the amount that the customer would have paid had it met its DS1 commitment.[112] Thus, under the Verizon West tariff, a party will only be

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111 CenturyLink is the only ILEC that allows this practice. As with Verizon's other Commitment Plans, the plan available in the Verizon West territory does not allow customers to apply purchases of Ethernet services towards its minimum purchase commitment. A similar restriction exists in the Frontier tariff as well.

112 Verizon F.C.C. Tariff 14, Section 5.6.14(I) (For DS1s, "[w]hen the number of TVP DS1 SALs at the annual review is less than the commitment quantity minus 3%, the penalty will be the lowest TVP rate for the current threshold in the states where the service is located, multiplied by the shortfall multiplied by 4 months."). Verizon F.C.C. Tariff 14,

penalized for failure to comply with an obligation that was voluntarily assumed. XO still incurs substantial penalties pursuant to the Verizon West tariff when it falls short of its DS1 commitments. For example, in **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon West imposed an annual shortfall penalty of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** when XO failed to meet its DS1 purchase commitments by **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** circuits.[113] However, these penalties are not unreasonable and are somewhat similar to those imposed by competitive providers and stand in contrast to the excessive penalties XO has faced when it cannot meet the minimum commitments imposed upon it by Verizon North and South and AT&T, which result in a windfall for the two ILECs. The Frontier tariff similarly provides for a DS1 shortfall penalty only if the customer fails to meet the minimum purchase amount the customer selected at the outset of the term.[114] That penalty, however, like the Verizon West penalty for DS1 shortfalls, is only one-third of the expectation damages.

XO finds the contract option described in the CenturyLink tariff even more reasonable. Because there is no minimum commitment in the agreement, CenturyLink will not seek to

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Section 5.6.19(F) ("When the average number of in-service DS3 SALs at the Annual Review is less than the Minimum DS3 Commitment Quantity, … a shortfall penalty applies. The shortfall penalty is calculated by multiplying the following: (i) TVP rate for the predominant service type purchased by the customer … by (ii) The Minimum DS3 Commitment Quantity minus the average in-service quantity of DS3 SALs by (iii) twelve (12) months.").

113 Chambless Tariff Investigation Declaration ¶ 24.

114 *See* Frontier F.C.C. Tariff No. 5, Section 5.6.14(I).

impose or enforce a shortfall penalty if the purchaser does not purchase a certain amount of the qualifying services in any given period of the agreement. This type of commercial fairness and reasonable dealing is noticeably absent from the terms of the Verizon and AT&T commitment plans.

VIII. COMPETITIVE PROVIDER PLANS DO NOT HAVE SIMILAR LOCK-UP TERMS AND CONDITIONS AS THE ILEC PLANS

XO also has entered into agreements with CLECs to purchase Dedicated Services. In all instances, it has found the terms and conditions in these agreements are just and reasonable since they were entered into between parties with relatively equal bargaining power.

A. <u>CLEC DSn plans do not have the same types of lock-up provisions as ILECs</u>.

In entering into agreements with CLECs, XO normally does not commit to terms longer than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** to get their best rates. As discussed above, under the price cap ILECs' Commitment Plans, XO needs to agree to three, four, five, or seven years of a minimum commitment. For example, XO purchases Type II services from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. A similar agreement between XO and **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

Moreover, other providers' plans generally do not have minimum commitments or shortfall penalties. For instance, pursuant to the MSA between XO and **[BEGIN HIGHLY**

CONFIDENTIAL] [redacted] **[END HIGHLY CONFIDENTIAL]**

Similarly, the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL**], not a recurring shortfall penalty until the agreement is completed, as in the case with the ILECs. Despite these key differences, the circuit rates offered by competitors are typically much lower than what XO obtains from price cap ILECs even given the discounts in the Commitment Plans.[115]

When agreements with competitors other than price cap ILECs expire, month-to-month rates often apply – this is the case for XO's agreements with **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. Typically, these rates are at the same level as those in the expired deal under evergreen provisions which

115 *See* Section III.A, *supra* (discussion of comparison between ILEC and competitive provider wholesale rates).

apply while new arrangements are negotiated. In XO's experience, even where the contract with a competitive provider would allow the assessment of higher rates upon termination, competitive providers often do not invoke those provisions. This prevalent practice stands in contrast to the provisions of Verizon and AT&T plans, which use escalated month-to-month rates at the time of expiration and which effectively force competitors into a new long-term commitment tying up the bulk of a carrier's special access requirements.

B. XO's DSn plans do not have the same types of lock-up provisions as ILECs.

Unlike with the Verizon and AT&T Commitment Plans, XO does not impose volume commitments or lock-up provisions in retail and wholesale arrangements offered to its own customers. That is not to say that XO never negotiates larger discounts as a customer's overall volume increases or for longer terms, but, like other competitive providers, XO does not impose unreasonable minimums, maximums, or penalties. XO's arrangements with its retail and wholesale customers reflect what one would expect from providers under competitive conditions, where better prices reflect larger volumes of purchases (or the potential for future additional purchases). The fact that Verizon and AT&T do not offer such reasonable terms and conditions strongly suggests that, unlike XO and other competitive providers, they do not feel competitive pressure from their rivals in the market.

XO's terms and conditions differ markedly from Verizon and AT&T Commitment Plans. XO has standardized terms that govern most service order arrangements, which it posts on its website. With carrier and large enterprise customers, XO may enter into national MSAs, which are individually negotiated and often have customer-specific terms and conditions. Once the MSAs are in place, XO's customers can place orders for circuits at locations, the term and price of which may be individually negotiated as well. XO's commercial and carrier customers may commit to buy a certain number of circuits for a certain period to obtain a given price, but the terms and conditions of the arrangement are materially different than the Verizon and AT&T Commitment Plans. The arrangements XO enters into with its customers involve rather short term commitments (typically one to three years), and customers do not face punitive shortfall penalties for failure to meet minimum commitments. That said, to get the prices they negotiated, XO's customers must make the purchases for which they bargained. Further, XO never requires a customer making a volume commitment to purchase a certain percentage of its total requirements from XO or a percentage of its in-service circuits in place at the start date of an MSA. Rather XO negotiates the price at new locations based on the number of circuits the customer purchases at the locations, without reference to what its overall requirements are or its prior purchase history has been. XO does not have loyalty agreements. Where there is a deal involving a certain volume or term purchase, XO has no ability in negotiations to impose downturn provisions of the sort XO is subject to in its agreements with price cap ILECs. To the contrary, XO may **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[116]

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[116] There is typically a disconnect between the circuit contract XO enters into with its customers and the Commitment Plan that XO has with a price cap ILEC for the same circuit. XO cannot pass through onerous terms of the price cap ILEC Commitment Plans onto its own customers. In particular, the terms under which XO buys its wholesale inputs are less advantageous than the terms under which it sells the very same inputs to

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C. Even if CLECs offer contract terms similar to those offered by Verizon and AT&T, it is not evidence that the terms and conditions in these ILECs' plans are just and reasonable.

On the surface, some of the MSAs or isolated terms and conditions offered by XO and other competitors may appear similar to the Commitment Plans utilized by Verizon and AT&T (particularly with respect to term commitments and early termination liability clauses). However, by viewing these agreements in context, it is apparent why the terms and conditions in the Verizon and AT&T plans are unjust and reasonable while the CLEC agreements are not. As discussed extensively herein, competitors do not have the same ubiquitous network presence and resulting market power in providing Dedicated Services as Verizon and AT&T. This means that

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its customers. XO's carrier customers demand short terms from XO – typically one-year – because technology, equipment, and other aspects of the communications environment change so rapidly that anything longer would be imprudent. Moreover, customers wish to retain their ability to move to other providers on a short turn-around basis if they feel XO (or another provider) does not continue to offer the best deal. This dichotomy prevents XO from fully covering the risks of the underlying circuits due to the Commitment Plans. This may be because, reflecting the market conditions in which XO competes, the duration of the term of XO's agreements with its customers is shorter than that of the underlying circuits XO purchases from the price cap ILECs under the special access commitment plans. This is to say nothing of the additional risk under the Commitment Plans associated with failure to meet volume minimums. XO, unlike the price cap ILECs, does not have the market leverage to impose such terms.

Because larger enterprise customers often have competitive choices and XO does not have market power, XO's customers are able to push more and more of the risk onto XO, which has minimum commitments with the underlying price cap ILECs. Customers treat XO's off-net service no differently than on-net service provided using XO's own facilities. XO cannot offer its off-net services, with the increased costs and risks under the Commitment Plans, at different rates, terms, or conditions than on-net services in an effort to pass through those underlying costs and risks. If XO does attempt differentiation, customers tend to "cherry pick" the on-net services, making it that much more difficult to meet its minimum commitment.

when a customer chooses to purchase services from a CLEC, that customer would almost certainly be able to obtain the same services from either an ILEC or an alternative competitor, which is important for a number of reasons. First, unlike a CLEC's customers, the majority of the time, a competitive carrier seeking to sell TDM services on a wholesale basis can obtain them only from the ILEC. As such, competitive carriers are forced to accept the unjust and unreasonable terms imposed by Verizon and AT&T, while that same CLEC's customers could look elsewhere to obtain services if the CLEC's contract terms were likewise objectionable. Second, because CLECs are present in only a small fraction of the buildings in any given metro area, the presence of contract provisions in a wholesale agreement that seemingly impose term commitments and early termination liability is not necessarily a reflection that competitors are on equal footing with Verizon and AT&T. Rather, these are typically standard contract terms that are included in most MSAs, including XO's, unless a customer specifically objects to them.[117] If a customer asks a competitive carrier to remove these terms, the carrier will typically acquiesce to such a request or risk losing the customer to another competitive carrier, or, more likely, to the price cap ILEC. Moreover, even if such terms are present in an MSA, CLECs often forego enforcing them as a strategy to retain its customers and remain competitive in the market. Finally, the real issue in the Verizon and AT&T Commitment Plans is the shortfall penalties combined with the percentage-based commitments. The CLEC agreements do not contain these

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[117] *See* Anderson SA Declaration ¶ 38 ("For smaller commercial customers, XO has standardized terms which govern most service order arrangements. If necessary, XO will negotiate special arrangements. With carrier and large enterprise customers, XO enters into national master service agreements ("MSAs"), which are individually negotiated and often have customer-specific terms and conditions.").

same objectionable provisions (even if they contain term commitments and early termination liability clauses, CLEC agreements would not have the same deleterious impact in the market because competitors do not have the same ubiquitous market presence as the ILECs).

IX. THE COMMISSION SHOULD GRANT RELIEF TO ENSURE THAT SPECIAL ACCESS DS1 AND DS3 SERVICE ARE AVAILABLE ON JUST AND REASONABLE TERMS

The previous sections demonstrate that key provisions of the Discount Plans of Verizon North and South and AT&T in each of its four regions that are under investigation are unjust and unreasonable. These provisions, especially the percentage minimum commitment provisions and the shortfall penalty provisions, should be held to be void and unenforceable. At the same time, the Commission, in the *Special Access Rulemaking*, should conclude that the month-to-month "rack" rates for Dedicated Services, except where new triggers for pricing flexibility have been met, should be reset at the lowest rate available under the Discount Plans.[118]

Should the ILECs, once the Commission resets the rack rates of the ILECs, wish to offer Discount Plans to offer even lower rates, such plans should be based upon traditional volume discounts, balancing the rates charged by the volume purchased, such as the contract described in CenturyLink's Tariff FCC No. 9. Percentage minimum commitment provisions should be treated as unreasonable *per se*. No shortfall penalties would be needed, as a result.

Finally, unlike the Verizon CDPs in its North and South regions, wholesale customers under a Discount Plan should be able to move circuits out of the plan should they choose to do so, whether to month-to-month rates, to UNEs, or to Ethernet service, a customer carrier's own

[118] *See* XO's *Special Access NPRM* Comments at 44-55.

facilities, or to those of an alternative provider. Given the technology transitions and growing transition of many special access customers to Ethernet services, volume discount plans should be considered reasonable only if they allow for migration of circuits from DSn to Ethernet services and still count toward the level that sets the discount. In such cases, the discount on circuits might change over time, but the wholesale customer would suffer no unreasonable shortfall penalties and risk paying for a customer's service twice, once for actual service used by its retail or wholesale customer and once more under a shortfall assessment periodically through the remainder of a Discount Plan's term.

Respectfully submitted,

Thomas Cohen

Lisa R. Youngers
XO Communications, LLC
13865 Sunrise Valley Drive
Herndon, VA 20171
Telephone: (703) 547-2258

Thomas W. Cohen
Edward A. Yorkgitis, Jr.
Kelley Drye & Warren LLP
3050 K Street, NW, Suite 400
Washington, D.C. 20007
Telephone: (202) 342-8400

Its Attorneys

February 5, 2016

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO
PROTECTIVE ORDERS IN WC DOCKET NO. 15-247
BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

DECLARATION OF MICHAEL CHAMBLESS

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the Matter of: Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plan	WC Docket No. 15-247

DECLARATION OF MICHAEL CHAMBLESS

1. My name is Michael Chambless. I have been employed at XO Communications, LLC ("XO") since June 2015. My current position is Vice President of Access Management and Planning with responsibilities predominately geared towards Telecom Expense, Carrier Relations and Access Planning and Implementation. I have been in this position since my employment with XO began.

2. In total, I have over 38 years of experience in the telecommunications field. I had a career in the United States Air Force and retired in 1994. During that period, I was responsible for the maintenance and operations of complex communications infrastructures. After retirement from the Air Force, I spent approximately 2 years working for a consulting firm predominately supporting Fortune 500 companies in areas of network engineering and implementation. My most recent position prior to XO was as Vice President of Network Shared Services and Support at CenturyLink reporting to the Executive Vice President of Global Operations. Responsibilities at that time included the direction of process teams supporting Network Planning,

Engineering/Construction and Operations; a team responsible for special projects and project management initiatives; another that performed budget management and analytics for the network capital expenditures; all internal corporate networks supporting the enterprise.

3. At XO, I oversee our overall procurement of (spend on) telecommunications services and ensure that we get the best rates for access circuits required to provide services at retail and wholesale to our customer base. Our planning teams regularly evaluate the circuits we have purchased and try to find less costly alternative circuits to which we can migrate customers, allowing for a better margin of profit. My responsibilities also include financial analysis and network optimization related to all forms of access services, including special access, unbundled network elements ("UNEs"), and Ethernet based services. This includes identifying and analyzing systems development projects for provisioning of all access services. In this capacity, I am involved in the purchase and negotiation of rates, terms, and conditions for special access services, including cost of service monthly and annual forecasting and maintenance of term plans and contracts.

4. The purpose of this declaration is to support XO's comments in the Federal Communications Commission's (the "Commission's") investigation of certain special access tariff plans of Verizon, AT&T, Frontier, and Century Link. I understand that in preparing its comments, XO will also be relying on the declaration ("Special Access Declaration") I executed on January 22, 2016, for use by XO in support of its January 27, 2016, comments in the Commission's WC Docket No. 05-25 (Special Access for Price Cap Local Exchange Carriers) and RM-10593 (AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent

Local Exchange Carrier Rates for Interstate Special Access Services). This declaration is written to supplement my Special Access Declaration.

5. XO prefers to provide over its network facilities dedicated time division multiplexing ("TDM") and Ethernet services (collectively, "Dedicated Services"), including any value added services in connection with those Dedicated Service, such as voice, Dedicated Internet Access ("DIA"), and interoffice networking. There are many reasons for this: more rapid provision of services, greater ability to innovate, higher network reliability and quicker repair, and better margins. As a result, XO has accelerated its investment in network facilities, including through its $500 million "On-Net Initiative" launched in 2014. But XO's on-net reach, even after this construction initiative is completed, will still be limited to fewer than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** buildings nationwide. In any one of the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Metro areas in which XO has Metro fiber rings today, XO access only a very limited number of commercial buildings with lateral facilities. For example, XO has lit fiber only to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

6. As I explained in detail in my *Special Access Declaration*, to serve its retail business and enterprise and wholesale customers, XO must have access to wholesale inputs, both TDM-based – DS1 and DS3 special access and unbundled DS0 copper loops – as well as Ethernet services from incumbent local exchange carriers ("ILECs') and competitive providers. As my *Special Access Declaration* explains in more detail, XO's arrangements with the ILECs to obtain

Dedicated Services are critical because the ILECs alone are connected to virtually all commercial buildings in Metro areas nationwide, while competitive facilities-based providers are available only in a small percentage of locations. The ILECs' volume and term Discount Plans under investigation by the Commission, therefore, are the key source of DS1 and DS3 special access services at rates that make it possible for XO to compete. XO is a customer of Verizon's Commitment Discount Plans for DS1 and DS3 services in both Verizon North and South territories, for example, under Verizon's FCC tariffs Nos. 1 and 11. In fact, of the DS3 circuits that XO purchases under ILEC Discount plans, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** are purchased from Verizon. XO is also a customer under each of the four AT&T Discount Plans for DS1 services that are under investigation in the Commission's proceeding. Finally, XO is a customer under the Verizon West Discount Plan being investigated (Verizon FCC Tariffs No. 14), and the Frontier Discount Plans in former Verizon West territories (Frontier FCC Tariff No. 5).

7. As detailed in my *Special Access Declaration*, even though, for the past two years, XO has received **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the volume of new and installed TDM services (especially DS1s) remains substantial. XO established its business by providing DS1 and DS3 TDM services, and many of its TDM customers continue to value the service, often because they can use and derive maximum value from their legacy equipment. In addition, many small-to-medium-sized business customers continue to find TDM-based service to be sufficient for their needs. These customers'

attachment to TDM holds true even though Ethernet prices are dropping and performance is increasing.

8. Thus, XO expects that DSn special access will remain important to competitive providers for years to come, although **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** As of year-end 2015, for example, XO still had almost **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** ILEC-provided special access DS1 channel terminations in place pursuant to the tariffs that are under investigation, and over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS3 ILEC-provided channel terminations as well. Further, although there has been a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** For example, XO's installed base of DS1s under its CDP with Verizon North declined from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** a decline of only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** The decline of DS1s in place in Verizon South is only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Declines in the Bellsouth region are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** In the PacBell

region, where XO had **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS1s installed as of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the decrease was **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Based on XO's internal projections, it anticipates approximately a net **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** decline in its requirements for new and installed DS1 circuits nationwide in 2016.

9. The decline in DS3s is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** In the Verizon North and South regions, where **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS3s under the Discount Plans being investigated are located, the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Yet, even these rates of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** mean that DS3s will remain important for several more years. More importantly, these rates of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** mean that XO will face shortfall penalties for DS3 circuits with **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** over the course of the new CDPs for DS1 and DS3 services in Verizon North and South regions entered into in October 2014.

10. Where competitive providers also have facilities to a building, their rates are typically **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** than the ILEC's. For XO, price is by far the most important factor in purchasing Type II facilities,

and where not otherwise constrained, as I will detail below, XO will purchase its Type II facilities at the lowest possible price. As a general rule, XO finds the ILEC discounted rates are higher than the on-net rates of alternative providers. I have reviewed on-net rates for competitive carriers that are among the largest providers of DS1 and DS3 services to XO (excluding the ILECs) in several key Metro areas in the Verizon North and South territories **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** and AT&T regions **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** As shown by the comparison in Highly Confidential Exhibit A appended to this declaration, the average competitors' rates in the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon cities (in buildings where the competitors have facilities) are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** below the rates of the ILEC for zero-mileage channel terminations. In the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** AT&T cities, average competitors' rates are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** below AT&T's zero mileage rates. When mileage charges are added for channel terminations that end in a remote central office, the difference becomes even more extreme. This is because Verizon and AT&T assess mileage charges while the CLECs do not. For instance, for a five mile charge, the competitors' rates in the Verizon cities are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** lower than Verizon's and, in the AT&T cities, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** lower than AT&T's. While these data reflect an average between two of the largest competitive providers' pricing for DS1 and DS3 circuits in these cities, XO finds that competitive facilities-based providers of DS1 and DS3 special access offer their services at rates within just a few percentage points of this average, not only in these cities, but in many other Metro areas as well (where present).

11. As a general matter, the Discount Plans under which XO purchases DS1s and DS3s contain minimum commitments expressed in terms of channel termination counts. If XO falls below the minimum commitment level for the period of time set forth in the Discount Plan, *e.g.*, one month, six months, or a year, XO will be assessed a shortfall penalty. This creates an incentive for XO to purchase enough DS1s and DS3s to meet its minimum commitment. As a consequence, to meet its minimum commitments and avoid shortfall penalties, XO often has no practical choice but to purchase special access from the ILEC under the Discount Plans, not only where the ILEC is the only provider in the building, but also when there are one or more alternative providers which offer a better rate. If it were to purchase from a competitive provider and suffer a shortfall penalty as a result, XO's costs of service would increase unacceptably. To avoid the shortfall penalties where XO is getting close to or is already under the minimum commitment, XO, were it to groom an existing customer's circuit to a competitive provider, would still have to purchase the ILEC DSn circuit over and above what it pays for any circuit from the competitive provider. The same holds true for new orders for DS1s and DS3s where competitive options are available.

12. The net result of the foregoing dynamic is that competitively offered options, even if less costly, are nonetheless commercially unattractive. Because reduced purchases under the Discount Plans combined with declining demand for DS1 and DS3-based services accelerates the

potential for imposition of shortfall penalties (i.e., significantly increased costs), **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

13. I understand that Verizon and AT&T in their submissions in the tariff investigation claim that carriers like XO that participate in their Discount Plans retain a considerable degree of control over the size of their minimum commitments. This has not been XO's experience when renewing its Discount Plans with these two carriers, in particular regarding the Verizon North and South CDPs and to a large extent with the AT&T Discount Plans. XO has found that there is limited or no opportunity for it to dictate what its minimum commitment will be. I should note that, because of the current overall declining demand for DSn services, XO finds that flexibility above the minimum commitment (and on overage charges) are not an issue – shortfall penalties are.

14. The Verizon CDPs in the old NYNEX and Bell Atlantic territories, i.e., Verizon North and South, respectively, require a carrier entering into the CDP to accept a minimum commitment of 90% of the in-service channel terminations as of the date of renewal. (*See* Verizon's Tariff FCC No. 1 and Tariff FCC No. 11.) XO's CDPs automatically renewed at the end of September 2014 with new minimum commitments.

15. Prior to renewal of its Verizon CDPs, XO made attempts to negotiate lower commitment levels and alter terms concerning the satisfaction of the minimum commitments.

XO also looked into moving circuits to other providers through such methods as assumption agreements or grooms. **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon CDP's in those regions required XO to purchase all DSn services under the CDP. Therefore, XO could not, for example, to address concerns about anticipated falling demand, replace special access circuits with UNEs at the end of its CDP term to lower the minimum commitment upon renewal. In the end, XO determined that it could not reduce its commitment in any significant way in a timely fashion and would incur increased shortfall penalties resulting from moving customers off underlying circuits purchased under the Discount Plans. As a result XO found it impractical to lower its minimum commitment upon renewal apart from the operation of the 90% term, which effectuated a 10% reduction. This locked XO into commitment levels of maintaining 90% of XO's inventory of DS1s and DS3s in the North and South regions as of September 30, 2014, or face shortfall penalties.

16. As the result of falling demand for DS1 and DS3 services, XO was already exposed to substantial shortfall penalties toward the end of the prior CDPs. Indeed, XO was assessed over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** dollars in shortfall penalties under its Verizon North and South CDPs between **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** An additional **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in penalties was assessed for the three-month period of **[BEGIN**

HIGHLY CONFIDENTIAL] [redacted] **[END HIGHLY CONFIDENTIAL]**

17. XO has had better, but still limited, success in the past few years with reducing its commitment level under the AT&T Discount Plans prior to renewal. XO's DS1 Discount Plans in three of the four AT&T regions – the old Ameritech, PacBell, and Southwestern Bell Regional Bell Operating Company territories – have **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** terms. (XO's plan with Bell South is for **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**) XO has been able to convert **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS1 special access circuits that were under the AT&T Discount Plans to UNEs, and it has been able to move them back to special access to stay above the percentage minimum commitment and avoid shortfall penalties as demand declines. Whether UNEs at the DS1 level are available depends upon the presence of appropriate ILEC facilities – copper DS1 facilities are much easier to access and utilize as UNEs than fiber DS1 facilities – as well as whether the Commission's impairment triggers have eliminated the ILECs' obligation to unbundle DSn circuits as UNEs in specific wire centers. As ILECs continue to retire more copper facilities, the availability of DS1 (as well as DS3 and DS0 copper loops) UNEs will become more problematic, pushing competitors to rely more on tariffed Discount Plans to obtain ILEC DSn wholesale inputs. However, at some point, as demand for DS1s continues to slide, any UNEs XO may have "in reserve" to convert in AT&T territories will be exhausted, and XO will eventually face shortfall penalties and increased costs.

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

18. XO entered into a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** DS1 commitment with Ameritech under a Discount Commitment Program ("DCP") Plan starting in October 2015. AT&T Ameritech allowed XO to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** which effectively, at the time of Plan renewal, removed them from the percentage minimum commitment level. However, XO's ability to move the circuits has been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Even after identifying **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Ameritech and XO are still working to convert identified the circuits **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** The delays arise for a variety of reasons, some attributable to both parties, including limitations on the pace of conversions permitted by the ILEC. Ameritech has been **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** This is the only time that an ILEC has extended such an accommodation to XO.

19. XO renewed its **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Discount Plan agreements with AT&T in March 2015 in the Southwestern Bell and PacBell regions. Prior to the renewals, XO converted **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of its DS1 special access

circuits to UNEs. XO is closely monitoring the numbers of DS1s that remain active under the Plans on a month-to-month basis to manage its commitment levels under those agreements.

20. In XO's DS1 agreement with BellSouth, XO receives a discount for a level of channel terminations to which it voluntarily commits. Charges for DS1s in region under the Plan that exceed that amount are charged at a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Accordingly, there is no "headroom" under the BellSouth Plan to exceed the razor fine minimum commitment.

21. XO faces a penalty under the ILECs' Discount Plans for failure to meet the minimum commitment which is always stated in terms of channel terminations. Yet the penalties under the various Discount Plans vary greatly.

22. For example, in the Ameritech region, the shortfall penalty is directly tied to "expectation damages," meaning a penalty designed to recover what would have been spent on channel terminations if the minimum commitment was met. In the Ameritech region, the measurement period for assessing whether the minimum commitment is met is a given month ("Month One"), but Ameritech provides a grace period should the number of in-service DS1s be at or above the minimum commitment three months later (i.e., by "Month Four"). In Ameritech, there are state-specific minimum commitments, in contrast with the region-wide minimum commitments in the other three AT&T regions. If the customer fails to bring the number of in active service DS1s above the minimum in Month Four, then the penalty is assessed for Month One equal to the number of channel terminations that make up the shortfall times the monthly

charge. As the demand for DS1 channel termination falls, the ability to take advantage of this grace period will diminish.

23. In some other ILEC regions, the penalty for a DS1 shortfall under a plan is less than the monthly rate, and therefore less than expectation damages. In the BellSouth region, unlike the Ameritech region, AT&T's shortfall penalty is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** per DS1 channel termination, which is less than the channel termination price.

24. Under the Frontier and Verizon West Discount Plans, the amount of shortfall, if any, is assessed over a twelve-month period. However, the penalty is not twelve times the monthly rate times the number of monthly average of channel terminations the customer falls short, but only four times. (In the case of DS3 plans in Frontier and Verizon West, by, the shortfall penalty is twelve times the monthly rate times the number of average channel terminations the customer falls short, i.e., expectation damages.) For example, in **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon West imposed an annual shortfall penalty of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** when XO failed to meet its DS1 purchase commitments by **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** circuits. Thus, Verizon West and Frontier assess a penalty much smaller than expectation damages for DS1s.

25. Other ILEC Discount Plans provide for penalties well in excess of expectation damages. In contrast with the other AT&T Regions, both Southwestern Bell and PacBell impose a shortfall penalty in the form of a $900 per DS1 channel termination for the number of channel

terminations, if any, the Plan customer falls short of the minimum commitment. This penalty, which is reassessed in the first month there is a shortfall, is several times the monthly charge for a channel termination. While the charge is labeled "non-recurring," unless XO is able to add a circuit to make up for the shortfall, the additional penalties will recur in successive months at the rate of expectation damages. (*See, e.g.*, AT&T Tariff FCC No. 1, Section 31.5.2.7.1(A) and 7.4.18(E)(4).) While XO might be able to **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** to make up for the shortfall in some instances, it often cannot do so. Even if the shortfall is closed in the following months, the customer would face the same $900 per DS1 if there is a subsequent shortfall. The Southwestern Bell and PacBell shortfall penalties are unreasonable because they bear no relationship to the charge for a channel termination and leads to an effective rate for any channel termination that is well above even the month-to-month rate. Such a penalty results in a potentially huge windfall for the ILEC.

26. The shortfall penalties in the Verizon North and South territories have proven to be **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the cost of the channel terminations making up the shortfall. XO has faced these penalties on **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon's penalties, as set forth in its Tariffs No. 1 and 11 and interpreted by Verizon, do more than provide for expectations damages when the customer fails to meet its minimum commitment, which is based solely on channel terminations, and measured over a six-month period. Rather than just include a charge of the number of channel terminations that make up the average monthly shortfall times the monthly

channel termination charges times the number of months in the measurement period, Verizon adds to the expectation damages measure an allocation of MUXing and mileage on the presumption that the customer were to purchase more zero-mileage channel terminations so as to remove the shortfall it would purchase these elements, by purchasing interoffice transport and channel termination with mileage, in the same proportion as well. This penalty greatly exceeds the expectation damages and is therefore "overloaded." (*See* Verizon FCC Tariff No. 1 § 25.1.7(B), ¶ 3; Verizon FCC Tariff No. 11 § 25.1.7(B), ¶ 3.)

27. For example, for the most recent measurement period under XO's DS3 CDPs from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon billed XO a total Shortfall Adjustment in its North and South regions of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** based on its interpretation of its tariffed formula. However, that penalty is almost **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of an expectation damages measure of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** based on the channel termination rate times the average monthly shortfall. *See* Highly Confidential Exhibit B, appended hereto. (In Verizon South, which involved the larger share of the total penalty, the shortfall penalty is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted]**[END HIGHLY CONFIDENTIAL]** of the full measure of "expectation damages.") For the periods **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon assessed even larger shortfall adjustments for DS3 services against XO, totaling more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** This amount is more

than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the amount that Verizon could expect to receive were XO to meet its minimum commitment. Indeed, the effective rate Verizon charges for the channel terminations that make up the shortfall are well in excess of Verizon's month-to-month rates which are, for example, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** higher than the discounted rates for DS1, well below the percentage increase represented by the shortfall penalties.

28. Verizon's "overloaded" penalties are unfair because the number of DS3 transport circuits XO purchases is independent of the number of DS3 channel terminations it purchases. XO uses those types of circuits for two different reasons – transport circuits for interoffice connects and channel terminations to connect XO equipment with end users, and does not combine them to serve the same customer. Historic data confirms the trends for these two categories of circuits are not coupled. Rather, when the number of DS3 transport circuits XO purchases change only a few percent from one period to another, the change in channel terminations is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** For example, in Verizon North, between **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the number of DS3 transport circuits fell only **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** but the total number of channel terminations over that same period fell **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** The comparison in Verizon South is almost as dramatic, a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** decrease

for DS3 transport relative to a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** decrease for DS3 channel terminations over the same period. Highly Confidential Exhibit C makes abundantly clear that the presumption of proportionality in Verizon's shortfall penalties between channel termination changes and mileage and MUXing charges is patently false.

29. Nor is there any proportionality between purchase of zero-mileage channel terminations and channel terminations with mileage. Moreover, more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the DS3 channel termination circuits XO purchased in the periods when there were shortfall penalties assessed in 2013 and 2014, for example, are standalone or zero-mileage circuits without any mileage charges. The high percentage of channel terms without mileage underscores the unfairness of basing the penalties above "expectation damages" predicated on zero mileage channel termination charges.

30. To minimize its potential shortfall exposure in Verizon North and South territories, XO has been working to move **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** even if in some cases the alternative may not be advantageous.

31. I understand that Verizon states in its submission in this proceeding that the shortfall penalties account for only a few percent of the ILEC's revenues under the CDPs. In XO's experience, the shortfall penalty for periods where the minimum commitment is not satisfied is typically much higher. For the **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** Verizon assessed DS1 and DS3 shortfall

penalties of **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** and the charges for the circuits actually purchased were **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** making the shortfall penalty over **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the charges assessed for actual services. When compared to the charges for channel terminations, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** the shortfall penalty for missing the minimum commitment to purchase channel terminations was **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the amount XO paid for channel terminations in the same period. In the earlier periods when Verizon assessed penalties, the size of the shortfall penalty was far more significant relative to the amounts paid for services than Verizon suggests.

32. Additionally, I understand that Verizon claims that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** However, this number does not match XO's records, which show the number to be **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** under the commitment plans.

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

I declare under penalty of perjury that the foregoing is true and correct.

Executed on February 5, 2016.

Michael Chambless

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

HIGHLY CONFIDENTIAL EXHIBIT A

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

Comparison of AT&T and Verizon DSn Channel Termination Prices to Competitive Vendor Prices in Select Major Markets

(% Difference = % Competitive Vendor Rate is below ILEC Rate)

[redacted]

[redacted]

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

HIGHLY CONFIDENTIAL EXHIBIT B

Verizon DS3 CDP Shortfall Penalties: January 2013 thru June 2013 Measurement Period

[redacted]

Verizon DS3 CDP Shortfall Penalties: July 2013 thru December 2013 Measure

[redacted]

Verizon DS3 CDP Shortfall Penalties: January 2014 thru June 2014 Measurement Period

[redacted]

Verizon DS3 CDP Shortfall Penalties: April 2015 thru September 2015 Measurement Period

[redacted]

**HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO
PROTECTIVE ORDERS IN WC DOCKET NO. 15-247
BEFORE THE FEDERAL COMMUNICATIONS COMMISSION**

HIGHLY CONFIDENTIAL EXHIBIT C

REDACTED - FOR
PUBLIC INSPECTION

Verizon North and South CDPs: Monthly In-Service Circuit Counts

[redacted]

Verizon North Comparison in DS3 Circuit Counts Jan 2013 to Sept 2014

[redacted]

Verizon South Comparison in DS3 Circuit Counts Jan 2013 to Sept 2014

[redacted]

HIGHLY CONFIDENTIAL INFORMATION – SUBJECT TO PROTECTIVE ORDERS IN WC DOCKET NO. 15-247
BEFORE THE FEDERAL COMMUNICATIONS COMMISSION

CENTURYLINK CONTRACT TARIFF PAGES

1801 California Street 10th Floor
Denver, Colorado 80202
303 992-5832
Mark.Brinton@CenturyLink.com

Mark Brinton
Manager

September 30, 2013

Transmittal No. 47

Secretary
Federal Communications Commission
445 12th Street, SW, TW-B-204
Washington, DC 20554

Attention: Wireline Competition Bureau

The accompanying tariff material, issued on behalf of CenturyLink Operating Companies (CLOC) and bearing Tariff F.C.C. Nos. 9 and 11, effective as reflected on the attached tariff pages, is sent to you in compliance with the requirements of the Communications Act of 1934, as amended.

The material consists of tariff pages indicated on the following check sheet(s):

9	41st Revised Page 1
	10th Revised Page 1.2
11	7th Revised Page 0-1
	4th Revised Page 0-1.27

The CLOC is filing one new contract tariff in Section 24 of Tariff F.C.C. No. 9 and four new contract tariffs in Section 24 of Tariff F.C.C. No. 11. The CLOC is filing these contracts under authority granted in Section 69.727 of the Commission's Rules and is in compliance with terms contained in Section 61.55 of the Commission's Rules.

In addition, under authority of Special Permission No. 13-021, two of the DS1 and DS3 Price Flex Contracts (No. 13-002 and No. 13-012) require concurrent subscription to the CenturyLink Operating Companies Tariffs F.C.C. No. 9, Contract No. 13-002 and F.C.C No. 11, Contract No.13-012.

Per Section 61.58 this filing is being made on not less than one day's notice.

In accordance with the requirements of Section 61.21(a)(3) of the Commission's Rules, the FCC Registration Number (FRN) for CenturyLink is 0018-6268-53. CenturyLink is filing this transmittal on behalf of issuing carriers on Attachment A.

The Application filing fee in the amount of $845.00 is being paid by credit card through the appropriate entries in Section E of the ETFS generated Form 159.

All correspondence and inquiries in connection with this filing, including service copies of petitions, should be directed to:

Mark Brinton
CenturyLink
1801 California Street, 10th Floor
Denver, CO 80202
Phone (303) 992-5832

Attachment: Tariff Pages

ATTACHMENT A

Federal Registration Numbers for
CENTURYLINK OPERATING COMPANIES

Tariff F.C.C. No. 9 Participants

0004-1465-85	0005-0517-68
0004-1404-22	0001-6851-48
0001-8252-98	0002-3825-70
0002-9015-51	0001-9523-40
0005-0517-43	0002-3825-70
0002-5952-47	0001-5666-94
0002-3420-38	0002-9388-43
0002-6434-35	0001-7701-22
0002-3372-44	0004-1839-19
0002-3916-39	0001-7770-36

Tariff F.C.C No. 11 Participants

003-7467-57
0008-1312-94 (Concurring Carrier)

ACCESS SERVICE

CHECK SHEET

Title Page, Supplement No. 1 and Original Pages 0-1 to 24-489 inclusive of this Tariff are effective as of May 1, 2013. (T)

PAGE	NUMBER OF REVISION EXCEPT AS INDICATED	PAGE	NUMBER OF REVISION EXCEPT AS INDICATED	PAGE	NUMBER OF REVISION EXCEPT AS INDICATED
Title	Original	0-1.25	Original	0-25	Original
0-1	7th *	0-1.26	Original	0-26	Original
0-1.1	Original	0-1.27	4th *	0-27	Original
0-1.2	2nd	0-2	Original	0-28	Original
0-1.3	1st	0-3	Original	0-29	Original
0-1.4	1st	0-4	Original	0-30	Original
0-1.5	Original	0-5	Original	0-31	Original
0-1.6	Original	0-6	Original	0-32	Original
0-1.7	Original	0-7	Original	0-33	Original
0-1.8	Original	0-8	Original	0-34	Original
0-1.9	Original	0-9	Original	0-35	Original
0-1.10	Original	0-10	Original	0-36	Original
0-1.11	Original	0-11	Original	0-37	Original
0-1.12	Original	0-12	Original	0-38	Original
0-1.13	Original	0-13	Original	0-39	Original
0-1.14	Original	0-14	Original	0-40	Original
0-1.15	Original	0-15	Original	0-41	Original
0-1.16	1st	0-16	Original	0-42	Original
0-1.17	2nd	0-17	Original	0-43	Original
0-1.18	Original	0-18	Original	0-44	Original
0-1.19	Original	0-19	Original	0-45	Original
0-1.20	Original	0-20	Original	0-46	Original
0-1.21	Original	0-21	Original	0-47	Original
0-1.22	Original	0-22	Original	0-48	Original
0-1.23	Original	0-23	Original	0-49	Original
0-1.24	Original	0-24	Original		

* New or Revised Page.

ACCESS SERVICE

CHECK SHEET (Cont'd)

PAGE	NUMBER OF REVISION EXCEPT AS INDICATED	PAGE	NUMBER OF REVISION EXCEPT AS INDICATED	PAGE	NUMBER OF REVISION EXCEPT AS INDICATED
24-462	Original	24-471	Original	24-480	Original
24-463	Original	24-472	Original	24-481	Original
24-464	Original	24-473	Original	24-482	Original
24-465	Original	24-474	Original	24-483	Original
24-466	Original	24-475	Original	24-484	Original *
24-467	Original	24-476	Original	24-485	Original *
24-468	Original	24-477	Original	24-486	Original *
24-469	Original	24-478	Original	24-487	Original *
24-470	Original	24-479	Original	24-488	Original *
				24-489	Original *

* New or Revised Page.

ACCESS SERVICE

24. CONTRACT TARIFFS

24.2 CONTRACT NO. 13-011 (N)

DESCRIPTION: Contract for Renewal of 2 DS3 Circuits

CONTRACT AVAILABILITY: Effective from October 1, 2013 through October 31, 2013

CONTRACT EXPIRATION DATE: 12-Months

AVAILABLE MSAS: MSAs identified in Section 23

This contract is for renewal of 2 DS3 circuits purchased on a 12-month Pricing Plan. The monthly rates for the discounted circuits shall be billed at the rates set forth below. All other rate elements and nonrecurring charges will be billed at the 12-month rates as set forth in Sections 7 and 17, preceding. Monthly rates for the entire 12-months will be frozen from Company-initiated rate changes.

Term Extension: On or before the expiration of this Agreement, the customer may extend this agreement for a 12-month period by notifying the Company in writing of its intent to do so. The customer may extend the Agreement a total of two times under the rates of this initial contract.

Total Monthly Rates the DS3 Circuits:

- Monthly Recurring Rates $2,215.68

The following eligibility criteria must be met in order to receive this Contract Offer:

- The customer must be renewing 2 DS3 circuits.
- The customer must be Federal Government.
- Service must be located in a Spokane, WA wire center: Spokane-Chestnut, WA (SPKNWACH).

If the customer elects to terminate service, prior to the end of the initial 12 month period, any previously waived NRCs will be assessed. (N)

ACCESS SERVICE

24. CONTRACT TARIFFS (N)

24.2 CONTRACT NO. 13-012

DESCRIPTION:	Existing DS1 and DS3 Services
CONTRACT AVAILABILITY:	Effective from October 1, 2013 through October 31, 2013
CONTRACT EXPIRATION DATE:	36-Months
AVAILABLE MSAS:	MSAs identified in Section 23

This contract tariff offers a Revenue Discount Simplification Plan for the Company's DS1 and DS3 Services, as set forth in Sections 7 and 17 preceding, (N) and which requires concurrent subscription to the CenturyLink Operating (N-x) Companies' F.C.C. No. 9 Tariff, Contract No. 13-002. Eligibility for these (N-x) discounts requires the customer meet or exceed the term revenue commitment of (N) $59,200,000.00 in Contributory Charges as set forth below.

TERMS AND CONDITIONS REQUIRED:

- The customer must meet or exceed a Term Revenue Commitment of $59,200,000.00. The Revenue Discount Simplification Plan is measured by totaling the net Contributory Charges for Contributory Services purchased during the 36-month term.
- Contributory Services may be comprised of DS1, DS3, SONET, Wavelength and Ethernet Service and other Special Access Services for the following (N) companies: CenturyTel (CT) ILEC, Embarq (EQ) ILEC, Embarq (N-x) Communications, Inc., (ECI), Lightcore, Qwest Communications Company (N-x) (QCC) IXC and Qwest Corporation (QC). (N)
- Contributory Charges are the customer's monthly recurring charges incurred during the term.
- Customers must currently subscribe to the Regional Commitment Plan (RCP) and have completed at least 24 months of the 48 month contract in order to be eligible to enroll in the Revenue Discount Simplification Plan.
- The Plan discounts per this Contract Tariff will only apply to DS1s and DS3 and must not exceed the billed charges. (N)

(x) Issued under the authority of Special Permission No. 13-021.

ACCESS SERVICE

24. CONTRACT TARIFFS

24.2 CONTRACT NO. 13-012 (N)
TERMS AND CONDITIONS REQUIRED: (Cont'd)

- The Company will calculate the customer's Contributory Charges that count towards the Revenue Discount Simplification Plan Credit within 30 calendar days following the end of a Measurement Period. The customer's first Measurement Period will begin on the first full calendar month after the implementation date, and each subsequent Measurement Period will be a calendar month. The customer's total Contributory Charges included on invoices with bill dates that occur within a Measurement Period will be included on a Contributory Charges Report and may include various bill dates during the calendar month.

- For each Measurement Period, the customer will receive a credit pursuant to the following Discount Tier Table. The applicable percentage will be applied to Month-to-Month Rates.

DISCOUNT TIERS

Tiers	Minimum Spend	Maximum Spend	Discount Percentage
1	–	$1,999,999	0.0%
2	$2,000,000	$2,699,999	15.7%
3	$2,700,000	$3,019,999	18.7%
4	$3,020,000	$3,499,999	20.7%
5	$3,500,000	$4,199,999	22.7%
6	$4,200,000	$5,199,999	23.7%
7	$5,200,000	$6,199,999	25.7%
8	$6,200,000	Above	27.7%

(N)

(x) Issued under the authority of Special Permission No. 13-021.

ACCESS SERVICE

24. CONTRACT TARIFFS

24.2 CONTRACT NO. 13-012 (Cont'd) (N)

AGREEMENT TERM AND TERMINATION

- Effective with the second Measurement Period, if the customer's Contributory Charges fall between the 5th and 15th percentile of the third discount tier, the parties agree to reset the Minimum and Maximum Spend of the discount tiers set forth above, so that the customer's Contributory Charges are positioned at the 15th percentile of the third discount tier. If the Contributory Charges fall between the 16th and 25th percentile of the third discount tier, no adjustments will be made to the Minimum and Maximum Spend. If the customer's Contributory Charges are greater than the 25 percentile of the third discount tier, then the Minimum and Maximum Spends of the discount tiers will be adjusted.

- If this Revenue Discount Simplification Plan is terminated prior to the customer meeting the $59,200,000.00 Revenue Commitment, then the customer will pay early termination charges equal to the Revenue Commitment less any net Contributory Charges paid for Contributory Services between the implementation date and 30 days after the date of the last invoice for Contributory Services.

- When the customer's net Contributory Charges for Contributory Services reaches $59,200,000.00 or greater, the customer may terminate the Revenue Discount Simplification Plan without incurring early termination liability charges.

- The customer may elect to extend the Revenue Discount Simplification Plan for two additional 12-month renewal periods by providing written notification at least 60 days prior to the end of the term or renewal term. The Revenue Commitment for the term extension will be reset at $19,700,000.00 for each one year renewal term. (N)

(x) Issued under the authority of Special Permission No. 13-021.

ACCESS SERVICE

24. CONTRACT TARIFFS

24.2 CONTRACT NO. 13-013 (N)

DESCRIPTION: Contract for a New DS3 Circuit

CONTRACT AVAILABILITY: Effective from October 1, 2013 through October 31, 2013

CONTRACT EXPIRATION DATE: 36-Months

AVAILABLE MSAS: MSAs identified in Section 23

This contract is a new DS3 circuit purchased on a 36-month Pricing Plan. The monthly rates and nonrecurring charges will be billed at the 36-month rates as set forth in Sections 7 and 17, preceding. Monthly rates for the entire 36-months will be frozen from Company-initiated rate changes.

If the customer elects to terminate service, prior to the end of 36 month period, the Termination Liability and Waiver Policy set forth in 7.1.8, preceding, will be waived.

The following eligibility criteria must be met in order to receive this Contract Offer:

- The customer must be purchasing a new DS3 circuit under a 36-months term plan.
- The customer must be Federal Government.
- The service must be located in a Denver-Boulder, Colorado MSA. (N)

ACCESS SERVICE

24. CONTRACT TARIFFS

24.2 CONTRACT NO. 13-014 (N)

DESCRIPTION: Contract - 12-Month Extension for One DS1 Circuit

CONTRACT AVAILABILITY: Effective from October 1, 2013 through October 31, 2013

CONTRACT EXPIRATION DATE: 12-Months

AVAILABLE MSAS: MSAs identified in Section 23

This contract is for the 12-month extension of one DS1 circuit at 60-month Pricing Plan rates as set forth in Sections 7 and 17, preceding. Monthly rates for the entire 12-months will be frozen from Company-initiated rate changes.

The following eligibility criteria must be met in order to receive this Contract Offer:

- The DS1 circuit extended must have been working for the previous 5 years at 60-month rates.
- Service must be located in Phoenix-Mesa, AZ MSAs: Chandler Main (CHNDAZMA), Chandler South (CHNDAZSO) and Chandler West (CHNDAZWE).

When the entire service or a portion of the service is disconnected prior to the expiration of the fixed period service rate plan then Termination Liability and Waiver Charges (TLA) as set forth in Section 7, preceding, will apply. (N)