

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matters of

VSNL Telecommunications (US) Inc.
Petition for Rulemaking

and

Assessment and Collection of Regulatory
Fees for Fiscal Year 2006

RM-11312

MD Docket No. 06-____

**COMMENTS IN SUPPORT OF
PETITION FOR RULEMAKING**

Level 3 Communications, LLC (“Level 3”) strongly supports the proposal of VSNL Telecommunications (US) Inc. (“VSNL”) to reform the Commission’s rules and policies governing the application of international bearer circuit (“IBCs”) to non-common carrier submarine cable operators.¹ Level 3 agrees with VSNL that IBC fee reform must occur now to rectify a punitive fee system that distorts the market for international broadband capacity.

Level 3 and its affiliates are leading providers of domestic and international Internet backbone and broadband capacity. With an advanced nationwide fiber optic system and metropolitan area fiber networks in the United States and Europe, Level 3 provides and uses large amounts of telecommunications bandwidth. To link its European and U.S. networks, Level 3 owns the Yellow System, a submarine cable system connecting landing stations in Brookhaven, New York and Bude, England, and it

¹ Assessment and Collection of Regulatory Fees for Fiscal Year 2006, VSNL Telecommunications (US) Inc. Petition for Rulemaking, RM-11312 (filed February 6, 2006) (“*VSNL Petition*”).

operates the system on a non-common carrier basis. Level 3 also owns or leases capacity on other submarine cable systems, both common carrier and non-common carrier. Level 3 pays IBC fees annually for active capacity on the Yellow System and for its leases on other systems.

As private submarine cable operators compete for customers requiring transoceanic capacity, the industry has experienced profound changes in the undersea cable capacity market that have quickly undermined the assumptions upon which the existing IBC fee system was based. International submarine cable capacity today is less often used by submarine cable operators for traditional two-way telephone traffic or the relatively low-capacity, jointly-provisioned private line services envisioned in traditional, jointly-owned common carrier submarine cable systems. Increasingly, large, unregulated Internet and other bandwidth-consuming companies seek to acquire massive amounts of international capacity from submarine cable operators, for their own business purposes.

These changes reflect the Commission's success in encouraging the development of submarine cable capacity through its private submarine cable policy. In *Tel-Optik*, the Commission predicted that "alternative private cable systems in which bulk capacity will be sold or leased on a non-common carrier basis would introduce more meaningful competition in the provision of North Atlantic transmission facilities" and that "this increased competition will ... further stimulate technology and service development to the benefit of international communications users."² As expected, unleashing companies to finance, build and operate private systems to supply bulk capacity to customers free of common carrier regulation has spurred the development of new technologies. At the

² *Tel-Optik Limited, Application for a License to Land and Operate in the United States a Submarine Cable Extending Between the United States and the United Kingdom, Memorandum Opinion and Order, 100 F.C.C. 2d 1033 (1985) ("Tel-Optik") at ¶ 18.*

same time, this capacity has accommodated the growth of high-tech networks such as the global Internet. These achievements have facilitated a remarkable advance in global commerce that has improved the economic prospects and consumer welfare throughout many parts of the world.

Unfortunately, the FCC has not applied its vision for increasing transoceanic capacity to the question of IBC fees, which remain firmly imbedded in the architecture of the low capacity systems described above. A predictable consequence of this success is that the glut of available submarine cable capacity (at least in the Atlantic Ocean region) has led to a decrease in bandwidth prices that far exceeded anyone's expectations. As intended, submarine cable users benefit from this vigorous competition. As suppliers compete vigorously to provide bulk capacity to bandwidth-intensive companies, their per-unit revenues shrink considerably. For example, Level 3 has seen prices for 2.5 Gbps drop by approximately 80% and 10 Gbps capacity drop by approximately 95% during the past five years. As prices drop, each cost element that cannot be passed through to the customer takes up a greater portion of the supplier's margins. IBC fees constitute one such element. Regulatory fees are the largest cost of selling high-speed international capacity. Attachment 1 contains a chart showing the relationship between regulatory fees and market lease prices for international submarine cable capacity. The chart shows that today's IBC fees, which are based on 2004 circuit counts, may constitute more than 50% of annual lease prices as determined in today's competitive market.

Applying the existing IBC fee regime to this capacity severely distorts the market for international broadband capacity and harms users. If suppliers pass IBC fees through to customers, the price of international capacity rises by up to 50-60%. This has the

effect of suppressing demand for international capacity. To the extent that suppliers cannot pass the costs through to customers, suppliers are forced to apply the IBC fees as a cost of doing business. In many cases, this makes the transaction demanded by customers uneconomical for the supplier, potentially suppressing supply.

Caught in this spiral of decreasing costs and increasing regulatory fees, and faced with poorly-defined requirements, some providers fail to pay any IBC fees. Although their rationale is unclear, their failure to pay may be based on their belief that IBC fees do not apply to submarine cable capacity used for the Internet backbone, or that they do not apply to capacity owned by or controlled by a non-U.S. entity. Regardless, the failure of any companies to pay applicable IBC fees raises the costs for those that comply by decreasing the number of units on which payment is based. This distortion provides a competitive advantage to those that fail to pay. These providers are trying to lower their costs basis and generate any type of profit at the expense of those who abide by the rules. Alternatively, they win more business against those that do pay, because they avoid IBC fees. Finally, by allowing companies to avoid their IBC fee payment requirements, the Commission will encourage (indeed force) companies to emulate the practices of the non-compliant few, resulting in a "race to the bottom" and eviscerating the regulatory fee system as it applies to all non-common carrier submarine cable providers.

Moreover, the broken IBC fee system lacks the predictability required for submarine cable operators accurately to charge their customers. In assessing fees on submarine cable systems, the Commission requires payment based on: (a) the total number of 64 Kbps equivalent circuits "active" for the paying carrier as of December 31 of the previous year; (b) the total number of 64 Kbps equivalent circuits "active" for all

carriers as of December 31 of the year before the count described in (a); and (c) the FCC's budget allocation attributable to providers of IBCs. Selling capacity during any given year, carriers must seek to recover IBC fees without being able to predict the IBC fee that will apply. In the supra-competitive international submarine cable capacity environment in which a few dollars can determine the customer's choice of vendor, having to guess at the company's liability for IBC fees forces a company to make critical decisions without necessary information. As a result, companies must choose among unattractive options: Winning the business by understating IBC fee liability while paying IBC fees and reducing expected margins; winning the business by understating IBC fee liability and underpaying IBCFs; or losing the business. IBC fees distort the market by rewarding regulatory risk-takers.

IBC fee timing further distorts the market by encouraging owners to base their capacity turn-up decisions on non-market factors. Because operators pay fees based on circuits that are active on a particular date – *i.e.*, December 31 of the previous year – they can avoid fees by activating circuits only at certain times during the year. For example, a capacity operator preparing to activate new capacity during December most likely can avoid substantial fee payments if it waits until January to activate the capacity. Customers and Internet-related businesses lacking necessary capacity in the later parts of a year might be forced to curtail business or raise prices based on supply constraints caused directly by the Commission's IBC fee program. The requirement to pay fees based on circuits that are active on a specific date results in a situation in which the IBC fee "tail" wags the international submarine cable capacity "dog".

Level 3 agrees with VSNL that the FCC is required to change the way that it assesses non-common carrier submarine cable operators for annual regulatory fees. As an initial matter, the FCC may only recover through regulatory fees its costs for "enforcement activities, policy and rulemaking activities, user information services, and international activities."³ These fees must "take into account factors that are reasonably related to the benefits provided to the payor of the fee by the Commission's activities..."⁴. If the Commission "determines that the Schedule requires amendment to comply with" this requirement, then the Commission "*shall* ... amend the Schedule of Regulatory Fees".⁵ VSNL has shown that the "Schedule requires amendment" to comply with the requirement that the Commission establish fees that account for "the benefits provided to the payor of the fee by the Commission's activities." In particular, VSNL has shown that the fees paid by non-common carrier submarine cable system operators no longer reflect the benefits to those operators of the Commission's activities.⁶ The Commission must amend the Schedule of Fees to account for this change.

In its proposal to bifurcate assessment of fees between common carrier and non-common carrier systems and reduce the portion for which non-common carrier systems are responsible, VSNL presents a reasonable way for the Commission to meet this statutory requirement. The Commission distinguishes between common carrier and non-common carrier submarine cable systems and imposes greater obligations on common carrier systems. Level 3 acknowledges that the International Bureau provides other services that benefit all international service providers regulated by the Commission, and

³ 47 U.S.C. § 159(a)(1).

⁴ 47 U.S.C. § 159(b)(1).

⁵ 47 U.S.C. § 159(b)(3).

⁶ *VSNL Petition* at 16-18.

that these services might be characterized as equally benefiting all regulated entities providing international services. While it is difficult to assess the quantitative difference in benefits received by common carrier as opposed to non-common carrier systems, what is clear is that by assessing the same fees on common carrier and non-common carrier submarine cable systems, the Commission violates Section 159(b)(1) because there is a quantitative difference in the amount of regulation imposed on non-common carrier as compared to common carrier submarine cable systems.⁷ Accordingly, the fee system must be changed in accordance with Section 159(b)(3). At a minimum, the Commission must reduce the regulatory fees applicable to non-common carrier systems. The first two elements of VSNL's proposal meet that requirement.

Strong public policy reasons also support VSNL's proposal. For almost 20 years the Commission has sought to encourage the deployment of competitive, innovative, high capacity facilities and advanced services through deregulatory decision-making. In addition to its pro-competitive measures in the submarine cable context, the Commission has acted forcefully to encourage new technologies in the domestic and international satellite⁸ and in the enhanced services⁹ context. In the *Triennial Review Order*, the Commission relieved incumbent LECs from their obligation to unbundled network elements under Section 251(c) of the Act partly "to ensure that both incumbent LECs and competitive LECs retain sufficient incentives to invest in an deploy broadband

⁷ Fees are to be determined, in part, by accounting for factors "reasonably related to the benefits provided to the payor of the fee by the Commission's activities, including such factors as ... shared use versus exclusive use ... and other factors that the Commission determines are necessary in the public interest." 47 U.S.C. § 159(b)(1)(A).

⁸ See, e.g., *Domestic Fixed-Satellite Transponder Sales*, 90 FCC 2d 1238 (1982), aff'd, *World Communications, Inc. v. FCC*, 735 F.2d 1465 (D.C.Cir.1984).

⁹ Amendments of Part 69 of the Commission's Rules Relating to Enhanced Services Providers, CC Docket No. 87-215, Order, FCC 88-151 (released April 27, 1988) at ¶¶ 16-20.

infrastructure".¹⁰ Most recently, the Commission deregulated the provision of the telecommunications component of broadband Internet access services in order to encourage the deployment of advanced broadband systems.¹¹ Here, as well, the Commission must reform its application of IBC fees in order to encourage the continued deployment of advanced, high capacity systems across the oceans. These systems are overwhelmingly used by Internet backbone, content and application providers that are leading the digital revolution and providing new opportunities for commerce and for low-cost information access across the globe. To ensure that the IBC fee regime does not undermine the beneficial growth of international capacity and competition in the submarine cable market, the Commission must establish a mechanism that balances market realities with the unique regulatory status and benefits provided by non-common carrier submarine cable systems.

Level 3 also supports VSNL's proposal to establish a flat, per-system fee for non-common carrier systems. Common carrier systems must file international circuit status reports, which the Commission uses to identify the number of circuits upon which to assess IBC fees. Non-common carrier systems do not file these reports, making it difficult for the Commission to assess the number of IBCs being used on non-common carrier systems. As explained above, moreover, Level 3 believes that some systems are not paying based on other asserted justifications and therefore would not pay (or possibly even report) even if they were subject to a reporting requirement. To address this issue, the Commission can either develop additional regulations that require private submarine

¹⁰ Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, CC Docket No. 01-338, Report and Order and Order on Remand, FCC 03-36 (released August 21, 2003) ("*Triennial Review Order*") at ¶ 541.

¹¹ Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, CC Docket No. 02-33, Report and Order, FCC 05-150 (released September 23, 2005) at ¶ 3.

cable providers to meet new reporting requirements or establish a mechanism that meets the same goals with instituting burdensome new regulations. Rather than establishing new reporting requirements (and thereby justifying additional fees), the Commission should develop a more simple approach that will provide for a *fair* assessment on *all* non-common carrier systems.

A flat fee provides simplicity and transparency, resulting in greater compliance without establishment of new regulations. The Commission has already recognized that a per-system approach would be simpler.¹² By assessing a flat fee based on easily-identifiable criteria, the Commission would not only make it easier for the Commission to assess and the industry to pay fees, but it would also incent and ensure compliance by all non-common carrier submarine cable systems landing in the United States. Providers would be able to predict year over year the amount of their fee, enabling them to price efficiently and accurately. Moreover, because the fees would no longer be based on active circuits on a date certain, they would have more incentive to place additional capacity on the market, keeping prices low and capacity flowing for global businesses. As a result, more providers would pay their fair share of regulatory fees, reducing the burden for other industry participants, limiting competitive distortion and reducing the Commission's workload.¹³ Level 3 would support extension of a flat fee system to all submarine cable providers.

¹² Assessment and Collection of Regulatory Fees for Fiscal Year 2004, MD Docket No. 04-73, Report and Order, FCC 04-146 (released June 24, 2004) at ¶ 29.

¹³ A flat fee system applied to all non-common carrier submarine cable systems would have the added benefit of capturing circuits owned and controlled by members of submarine cable consortia that do not have a regulatory presence in the United States but may use circuits for U.S.-related traffic. U.S. parties to such systems could pass these fees through to non-U.S. parties pursuant to construction and maintenance agreements.

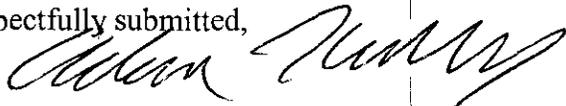
Moreover, a flat fee is consistent with the Act. As explained above, subsection (b)(3) requires the Commission to amend the Schedule to comply with subsection (b)(1)(a). The Commission may "add, delete or reclassify" services and may do so "to reflect ... changes in the nature of its services..."¹⁴ Nothing in these provisions would prevent the Commission from reclassifying non-common carrier submarine cables in another category and applying a flat regulatory fee to them. Under VSNL's proposal, the Commission would reclassify non-common carrier submarine cable systems outside of the "International circuits" category (including the bearer circuit requirement) and add it as a new service so as to reflect the unique regulatory characteristics of non-common carrier systems.

CONCLUSION

When the FCC set out to allow and encourage construction of private submarine cable systems, it correctly predicted that such a policy would lead to lower costs for bandwidth users. That premonition has turned out to be correct, and the FCC should take credit for its earlier decisions. However, as the competitive marketplace for international submarine cable bandwidth is teaching the industry, the benefits of the FCC's foresight are being lost through an antiquated regulatory fee recovery mechanism that has become increasingly punitive for those who choose to play by the rules. Unless the FCC acts immediately to reform its IBC fee recovery mechanism, the Commission will gut, through indifference, one of its greatest policy achievements. To prevent this unfortunate result, the FCC should grant the VSNL Petition and proceed quickly to fix the IBC fee system.

¹⁴ 47 U.S.C. § 159 (b)(3). The Act uses the word "services" in different ways. The only logical reading is that the first reference to "services" means the services set forth in the Schedule of Fees, and the second reference means the services provided by the Commission.

Respectfully submitted,



LEVEL 3 COMMUNICATIONS, LLC

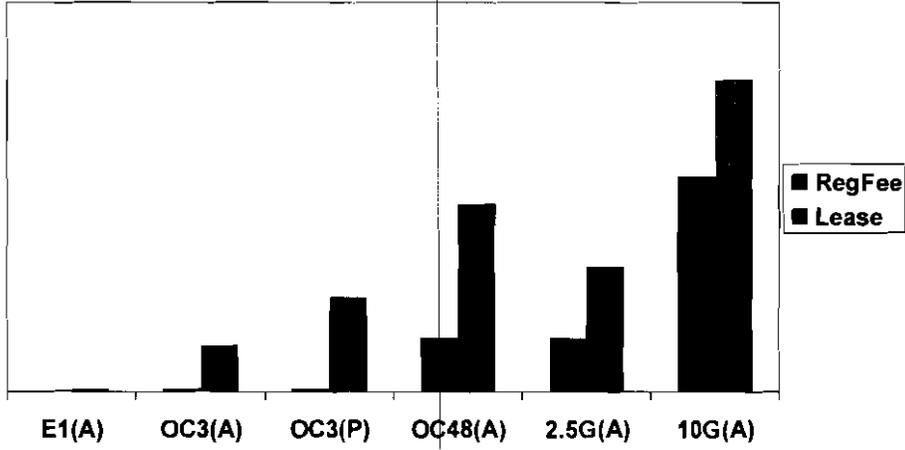
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Regulatory Fees as Percentage of Capacity Lease Grows with Capacity



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