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AUG 23 2012

Federal Communications Commission
Office of the Secretary



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Via ECFS and Hand Delivery

August 23, 2012

Marlene Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Room TW-A325
Washington, DC 20554

Re: Special Access NPRM, WC Docket No. 05-25 and RM-10593

Dear Secretary Dortch,

On behalf of Level 3 Communications, LLC ("Level 3"), enclosed are two (2) copies of the public version of a written ex parte, filed in accordance with the procedures outlined in the Protective Order in the above referenced proceeding.

In accordance with the Second Protective Order, all pages of this filing are marked "REDACTED - FOR PUBLIC INSPECTION".

Any questions relating to this submission may be directed to the undersigned.

Sincerely,

A handwritten signature in black ink that reads "Erin Boone" followed by a date "1/24/12".

Erin Boone
Level 3 Communications, LLC

Enclosure

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EX PARTE

August 23, 2012

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: Special Access NPRM, WC Docket No. 05-25 and RM-10593

Dear Ms. Dortch:

Level 3 Communications, LLC (“Level 3”) submits this letter to respond to Verizon’s most recent filings¹ attempting to convince the Commission that the special access market is not broken, or at a minimum, that any reforms must be put on hold, indefinitely, while the Commission gathers more data. Contrary to Verizon’s belief, the Commission has more than adequate data before it to find that the incumbents, including Verizon, have dominant shares of the special access market² and are uniformly engaging in unlawful contracting practices designed

¹ Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed Mar. 27, 2012) (March Verizon Letter); Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed Apr. 25, 2012) (April Verizon Letter); Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed May 2, 2012) (May Verizon Letter); Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed June 12, 2012) (June Verizon Letter); Letter from Evan T. Leo, Counsel for Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed July 16, 2012) (Verizon July 16 Ex Parte”); Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed July 17, 2012); Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed July 18, 2012).

² For the reasons stated in Level 3’s June 8 ex parte, the Commission need not find market power, but could easily do so. See Letter from Michael J. Mooney, General Counsel, Regulatory

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to maintain that dominance. Conservatively, total purchases of what the incumbent phone companies call “increasingly obsolete” local connectivity services are in the range of \$18 to \$20 billion annually. Sprint, a predominantly wireless company one would expect to be buying more and more Ethernet services, has said that it has hundreds of thousands of special access circuits deployed in its network, and in 2012, it expects to purchase tens of thousands of *additional* special access circuits.³ Put simply, these services are required and will continue to be required by every company that needs to move data between multiple locations around the nation. Lock-up terms and conditions tying up significant portions of this special access demand have no place in an allegedly competitive marketplace, particularly when employed by incumbents with dominant market shares. The Commission should act quickly to impose rules limiting the enforcement of existing exclusivity clauses and the execution of new ones. Under existing precedent,⁴ the Commission can do exactly that, and needs no further data to do so.

While Verizon’s most recent filings make no new arguments, one of the more perplexing aspects of its filings is its persistence in characterizing demand lock-up plans as “volume discounts,” particularly since they contain no volume requirements.⁵ Instead, Verizon’s plans require purchasers to commit between 85 and 92% of their existing number of Verizon circuits to Verizon regardless of the amount of “volume” such commitments produce. As Verizon has said previously, “[u]nder Verizon’s CDP, a customer who purchases just 14 DS1 channel terminations from Verizon can receive the same level of discounts as larger volume customers who subscribe to the CDP for the same term of years.”⁶ But Verizon has never answered the following question: if the customer committing to purchase 14 DS1s can get what is characterized as a “volume discount” for buying 14 DS1’s, then why can’t a customer purchasing 16 DS1s (or 100, or 1,000 or 1,000,000) get the same discount for also agreeing to maintain 14 DS1s with Verizon? If a discount is cost justified when one company buys 14 DS1’s, why is it not also cost justified at the 14 DS1 level for another company which happens to buy more than 14 DS1’s?

Policy, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed June 8, 2012) (“Level 3 June 8 Ex Parte”).

³ Letter from Charles W. McKee to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, WT Docket Nos. 05-25 and 02-55 (filed May 29, 2012), p.2.

⁴ See e.g., *Exclusive Service Contracts for provision of Video Services in Multiple Dwelling Units and Other Real Estate Developments*, Report and Order and Further Notice of Proposed Rulemaking, MB Docket 07-51, (Oct. 31, 2007), at ¶¶ 37, 4 (“*Exclusive Service Contracts Order*”).

⁵ See Verizon July 16 Ex Parte at 2-3. 5-6.

⁶ Letter from Donna Epps, Vice President, Federal Regulatory Affairs, Verizon to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (August 16, 2010) at p. 8.

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The answer is simple—it is because true volume discounts do not have the effect of limiting competition. Loyalty discounts, on the other hand, in which customers receive discounts not for the volumes they buy but for their agreement not to buy more than a fraction of their needs from competitors, do limit competition, and that is why they are used instead of volume discounts. Until these practices are declared illegal, they will continue to be used by dominant suppliers, and they will, as they have historically, continue to impede the special access market from beginning to become competitive.

Verizon claims that at the expiration of a lock-up plan's term, customers can either renew the plan or chose a new plan "but at a lower volume."⁷ Level 3 is not sure how that is accurate. Each of Verizon's lock-up plans requires a commitment of 85, 90% or 92% of the circuits in place with Verizon at the time the plan is entered. As such, Level 3 does not see how a customer can elect a "lower volume" under these plans. Were it truly Verizon's intention to offer a lower tier of commitment under its lock-up plans, it would be very easy for Verizon to draft such an option. But it hasn't, and Level 3's bet is it won't absent Commission intervention.

Instead of having in place a simple plan election for a lower volume threshold, Verizon points to ways in which a customer can obtain a lower commitment in a lock-up plan, provided the customer is willing to engage in contractual gymnastics *and* pay Verizon a huge penalty to do so. Verizon's plan in this regard involves a complicated undertaking in which, at the end of an existing lock-up plan's term, a customer places *some* of the previously committed circuits into a "term only" (*i.e.*, non-lock-up) plan—then at a later time, converts these "term only" plan circuits back into one of its a 85 to 92% lock-up plans, thus applying the same onerous lock-up percentages, but to a lower overall number of circuits.⁸ Presumably, this conversion would need to wait until after all of the circuits *not* put into the "term only" plan have been migrated away from Verizon or terminated—otherwise, they would be swept into the new lock-up plan.

Verizon does not mention that under its plan for achieving a "lower volume commitment," every circuit *not* immediately put into a "term-only" plan will see its pricing at least double as the result of the loss of the prior lock-up plan's discount (assuming a 50% discount) until it is moved away from Verizon. This would result in huge penalties being paid to Verizon if any meaningful number of circuits were being moved. Using simple numbers to demonstrate the impact, assume a customer had 20,000 DS1 circuits in a Verizon lock-up plan, and was paying \$150/month per circuit for them. At the end of the lock-up plan's term, assume it employs Verizon's idea, and moves 10,000 circuits into a term-only plan, leaving the other 10,000 "naked" (*i.e.*, no plan) intending to self-provide them or migrate them to a competitor. The price of those "naked" circuits would double, to \$300/month/circuit as the result of the lost discount, and beginning in the first month after the discount was lost, the customer would pay

⁷ Verizon July 1 Ex Parte at 4.

⁸ Verizon July 16 Ex Parte at 5.

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Verizon \$1,500,000/month *more* for the exact same services it was buying previously for \$1,500,000/month *less*.

No carrier can absorb these sorts of monthly increases in network expense without receiving anything whatsoever by way of corresponding value in return. Further, while these penalty payments would decline over time as circuits were actually migrated, Level 3 estimates that it would, realistically, take between [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] months to migrate 10,000 circuits.⁹ Assuming a straight line glide path (*i.e.*, an even number of circuits migrated each month) over a [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] month migration period, the penalty payments payable under the above example would be approximately [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL]—for nothing. Level 3 buys approximately [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL]. [REDACTED] [END HIGHLY CONFIDENTIAL]. The same example would hold as well for DS3 circuits—the number of circuits would be smaller, but the cost of each circuit would be much greater.

Finally, the Verizon idea assumes that a carrier will know every circuit it plans to migrate or terminate, and every circuit it plans to keep with Verizon at the time a lock-up plan ends (so that each circuit is placed into the correct bucket as noted above). This decision is meaningful—once a circuit is placed into a “term-only” plan, the circuit cannot be disconnected without paying Verizon a substantial termination penalty, and the pricing for any circuits not put in a term plan (*i.e.* the “naked” circuits) would jump materially. This sort of circuit-by-circuit clairvoyance may be realistic for a company buying 14 circuits from Verizon, but it is not reality for carriers buying thousands of them, particularly where the circuits are used in a wholesale business and resold to multiple end users whose needs regularly change over time.¹⁰ The “Verizon plan” for achieving a lower commitment level is simply unworkable in reality for any large Verizon customer, and results solely from Verizon’s unlawful lock-up contracting practices it refuses to change.

The foregoing approach for achieving a lower commitment level is obviously far more complicated and far more expensive than it needs to be if Verizon seriously intends to offer its customer’s a lower volume option. Level 3 believes this complexity and expense is intentional--

⁹ Verizon also points to its lock-up plans offering a two month extension before the plan is either automatically renewed or the plan’s discounts are eliminated. It is unrealistic to believe that any significant number of circuits could be ordered from and delivered by alternative providers in two months.

¹⁰ As Level 3, others, and even Verizon have recognized, the changing needs of end users is one of the reasons the flexibility of the price-cap LEC’s lock up plans is important to wholesale customers like Level 3, and why inflexible term-only plans are largely unworkable.

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Verizon makes it both really complicated, and really expensive for its large customers to extricate themselves from the grip of its lock-up arrangements, all in an effort to keep them in place so as to limit competition.

Verizon wants the Commission to believe that the evidence Level 3 has provided (at the Commission's request) demonstrating that: 1) Verizon's prices to identical locations are higher than CLEC's prices and 2) that Verizon's term commitments are much longer than those of CLECs doesn't mean anything. Level 3 disagrees. The evidence provided, when layered on top of the mounds of other, independent evidence demonstrating that the special access market lacks competition, clearly demonstrates the complete lack of meaningful competition in the special access market. The price-cap LECs lock-up arrangements are a major reason why.

Verizon also attempts to justify its longer term commitments by claiming that they result in greater discounts.¹¹ This is true, is part of the price-cap LEC's overall competition limitation strategy, and is one of the major problems Level 3 has noted over and over again with respect to the price-cap LEC lock-up plans since the inception of this debate. Verizon sets "list prices" for special access services (which virtually no-one pays) at astronomically high rates, then offers a huge "discount" off of those "list prices" to carriers that commit to buy all or almost all of their special access services from Verizon rather than from its competitors. A customer needing to buy *some* connections from Verizon (and every large customer does given that Verizon is the only game in town for large portions of its territory) will see its overall pricing skyrocket unless it commits to buy nearly all of its connections from Verizon in exchange for the discount. Given this "choice," it is not surprising that most large customers commit to buy the vast majority of their special access service from Verizon in region, all of which demonstrates the unlawfulness of the lock-ups. The price-cap LECs use their dominance to perpetuate their dominance, which is just wrong. And making matters worse-- the resulting rates being charged by Verizon, even after these "larger discounts," are still well above the rates of competitive providers where they exist. The magnitude of this pricing discrepancy is before the Commission.

Finally, Verizon appears to claim that Level 3's evidence of competitive pricing is also evidence that "competitive alternatives do exist at many locations."¹² As of this filing, Level 3 purchases **[BEGIN HIGHLY CONFIDENTIAL]** [REDACTED] **[END HIGHLY CONFIDENTIAL]** of its DS1 special access service needs from the price-cap LECs. Similarly, Sprint filed an ex parte on April 24, 2012 (in opposition to the Verizon Wireless/SpectrumCo transaction) in which it said that approximately 90% of its existing TDM DS-1s are still provided by incumbent LECs.¹³ The fact that vocal, large customers of the price-cap LECs like Level 3

¹¹ Verizon July 16 Ex Parte at 6.

¹² *Id.* at 7.

¹³ See Letter from David H. Pawlik, Counsel for Sprint Nextel Corp. to Ms. Marlene H.

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and Sprint continue to begrudgingly purchase the vast majority of their special access needs from price-cap LECs is clear evidence of a lack of competition as well as a problem in desperate need of a solution.

Sincerely,

/s/ Michael J. Mooney

Dortch, Secretary, Federal Communications Commission, WT Docket No. 12-4 (filed April 24, 2012) at 2.