

August 21, 2013

**VIA ECFS**

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

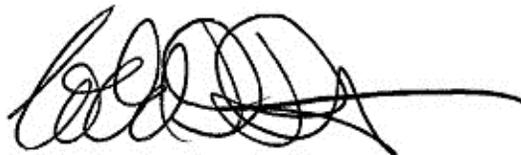
**Re: *Notice of Ex Parte, Telephone Number Portability, et al.*  
CC Docket No. 95-116; WC Docket Nos. 09-109 & 07-149**

Dear Ms. Dortch:

The Co-Chairs of the NAPM LLC received the attached letter on Friday, August 16, 2013. For the sake of transparency, I am filing the letter on behalf of the NAPM LLC in the above-referenced dockets.

Please contact the undersigned with any questions.

Sincerely,

A handwritten signature in black ink, appearing to read 'Todd D. Daubert', with a long horizontal flourish extending to the right.

Todd D. Daubert  
*Counsel for the NAPM LLC*

ATTACHMENT

FIRM / AFFILIATE OFFICES

Abu Dhabi	Milan
Barcelona	Moscow
Beijing	Munich
Boston	New Jersey
Brussels	New York
Chicago	Orange County
Doha	Paris
Dubai	Riyadh
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Houston	Silicon Valley
London	Singapore
Los Angeles	Tokyo
Madrid	Washington, D.C.

August 16, 2013

**VIA EMAIL & FEDERAL EXPRESS**

Melvin Clay  
AT&T  
675 West Peachtree Street, NW  
Atlanta, GA 30375

Timothy Decker  
Verizon  
600 Hidden Ridge  
Irving, TX 75038

**Re: Selection of the Next LNPA(s) and Negotiation of the NPAC Contract**

Dear Messrs. Clay and Decker:

I am writing to you as co-chairmen of NAPM LLC on behalf of a client who currently is, and in the recent past has been, a shareholder of companies that are members of NAPM. My client believes that NAPM, through the ongoing vendor selection process for the next Local Number Portability Administrator(s) (“LNPA(s)”), has an opportunity to meaningfully reduce the cost of the next Number Portability Administration Center contract (“NPAC Contract”). In particular, the current LNPA, Neustar, Inc., has earned exorbitant profits—to the detriment of NAPM members’ shareholders and customers—well above the level intended under the original NPAC Contract or for contracts involving government oversight more generally. On my client’s behalf, I therefore urge you to take measures to address these concerns in conjunction with the awarding and pricing of the next NPAC Contract—particularly as NAPM solicits and receives best and final offers from participating vendors—and I ask that you forward this letter to the NAPM Board for its consideration.<sup>1</sup>

Using Neustar’s publicly available financial disclosures, my client has calculated a reasonable estimate of Neustar’s revenues and profitability in the most recent years under the existing NPAC Contract. These figures, which are summarized in the attachment accompanying this letter, are striking. For example, in 2014, as you are well aware, Neustar’s NPAC revenues will reach \$466 million. More important, as you may not be aware, we estimate that Neustar will earn operating profits of approximately \$300 million on this contract in 2014—an operating

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<sup>1</sup> On behalf of my client, I have separately shared these concerns and the accompanying financial analysis with senior management of certain NAPM members.

profit margin of more than *60 percent*, and even higher when based on EBITDA. By comparison, NPAC fees totaled \$69 million in 2002 according to Neustar regulatory filings.<sup>2</sup> While the complexity and activity levels associated with the NPAC have increased over that time period, it is clear that the revenues and profits earned by Neustar since that time have deviated enormously from what a reasonable profit should be for providing a service that simply does not require complex technology or substantial capital, as evidenced by the fact that, prior to a large acquisition completed in late 2011: (i) Neustar was spending only approximately \$15 million per year on R&D, only a portion of which was attributable to the NPAC, and (ii) Neustar's net PP&E was under \$100 million, only a portion of which is attributable to the NPAC.

Neustar's extremely high profit margins are the unintended consequence of a number of factors, which NAPM has the opportunity to correct when it selects the next LNPA(s) and negotiates the successor NPAC Contract. *First*, contrary to the preference of the Federal Communications Commission ("FCC") and the best efforts of NAPM's members during the initial vendor selection process, Neustar has operated as the sole LNPA throughout the life of the current NPAC Contract.<sup>3</sup> Neustar thus has held a monopoly in its role as the LNPA for approximately 15 years, absent any competitive pressures to drive down costs or increase operational efficiencies.

*Second*, the quasi-fixed fee arrangement that NAPM implemented in 2009, and pursuant to which Neustar is paid under the existing NPAC Contract, is not in any way tied to a reasonable measure of Neustar's costs, but instead is the product of a legacy transaction-based pricing model run amok. As initially conceived, the LNPA's responsibilities were limited to facilitating *inter*-service provider porting to enable consumers to retain their telephone numbers when they switched to a competing provider. Under that initial conception, Neustar was to be paid on a per-transaction (or per-port) basis. Neustar argued at the time that telecommunications carriers could achieve network efficiencies if they used the NPAC database—and Neustar—for *intra*-service provider porting as well, which, not surprisingly, led to an explosion in the number of porting-related transactions, each of which generated new revenue and profits for Neustar. After several years of rapid growth in porting transactions, and under pressure to curb the costs associated with such growth, Neustar eventually agreed to the current quasi-fixed fee arrangement. But in so doing, Neustar effectively locked in an overly generous fee structure for the remainder of the existing NPAC Contract based on the revenues that were expected to be generated under the transaction-based model.

NAPM should make sure that negotiations are not in any way 'anchored' to price levels under the current contract which, as demonstrated above, are not a reasonable starting point. Indeed, Lockheed Martin—Neustar's former parent—and other government contractors typically

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<sup>2</sup> NeuStar, Inc., Registration Statement (Form S-1), at 32 (Mar. 29, 2005).

<sup>3</sup> See *Telephone Number Portability*, Second Report and Order, 12 FCC Rcd 12281 ¶ 38 (1997) ("[W]e agree, for the reasons given by the NANC, that there are clear advantages to having at least two experienced number portability database administrators that can compete with and substitute for each other, thereby promoting cost-effectiveness and reliability in the provision of Number Portability Administration Center services.").

generate profits in the 8 to 10 percent range. NAPM therefore should prevent Neustar from further entrenching itself as the LNPA monopoly by selecting multiple LNPAs as part of the ongoing vendor selection process. In fact, NAPM should consider selecting two or more vendors in each RBOC region, as Comcast has advocated before the FCC.<sup>4</sup> In addition, using the information provided in the attachment and Neustar's public disclosures, NAPM should drastically reduce the price of the next NPAC Contract, which would allow NAPM's members to pass the cost savings through to their customers and shareholders. NAPM members have a fiduciary duty to their shareholders and customers to give serious and thorough consideration to competing proposals, rather than simply extracting modest price concessions from Neustar that would once again yield excessive profits.

Please do not hesitate to contact me should you have questions regarding any of the foregoing information or the attachment.

Sincerely,



Matthew A. Brill  
of LATHAM & WATKINS LLP

Attachment

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<sup>4</sup> See generally Comments of Comcast Corporation, WC Docket No. 09-109 *et al.* (filed Sept. 13, 2012).

## EXPLANATION OF NPAC CONTRACT MARGIN ANALYSIS

- Neustar’s public disclosure breaks down its revenues into three operating segments: Carrier Services, Enterprise Services and Information Services. The NPAC Contract is contained in the Carrier Services segment, and constitutes the vast majority of the revenues in this segment.
- Neustar’s public disclosure also breaks down its direct operating expenses into the same three operating segments, resulting in a “Segment Contribution” for each segment that represents profits before indirect expenses.
- Consequently, in order to estimate the profits earned by Neustar on the NPAC Contract, one must estimate (i) the portion of direct operating expenses in the Carrier Services segment that should be allocated to the NPAC Contract, and (ii) the portion of total company-wide indirect operating expenses that should be allocated to the NPAC Contract. For item (i), since the vast majority of revenues in the Carrier Services segment are for the NPAC Contract, this part of the analysis should not materially affect the estimated margin.
- The following analysis contains a “High” and “Low” estimate for profits generated from the NPAC Contract. We believe the “High” estimate is a more accurate depiction, though we recognize that we are basing this analysis on imperfect information.
- The “Low” estimate assumes that direct operating expenses in the Carrier Services segment are allocable on a proportionate basis to revenues in the Carrier Services segment, and further assumes that indirect operating expenses are allocable on a proportionate basis to company-wide revenues.
- We believe this “Low” estimate understates the margins of the NPAC Contract because: (i) Neustar has indicated in the past that non-NPAC revenue streams in the Carrier Services segment, such as Order Management revenues, have significantly lower margins than the NPAC; (ii) indirect expenses include certain expense items which should not apply to the NPAC Contract, such as sales and marketing expenses (there should not be any ‘sales’ or ‘marketing’ required to run the NPAC) and corporate overhead (which would exist irrespective of whether Neustar operated the NPAC).
- Consequently, we also show a “High” estimate, which adjusts for the points made in the paragraph above by: (i) assuming that non-NPAC revenues in the Carrier Services segment have a 60% segment contribution margin (as opposed to approximately 87% for the Carrier Services segment as a whole), and (ii) deducting all sales and marketing expenses and an estimated \$25 million of corporate overhead from indirect expenses, before then allocating the remaining indirect expenses on a proportionate basis to company-wide revenues.

**ESTIMATES BASED ON PUBLIC DISCLOSURES**

**NPAC CONTRACT MARGIN ANALYSIS**

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>1H-2015</u>
<b>Revenues</b>					<b>Annualized</b>
NPAC Fixed Fee	\$ 366	\$ 411	\$ 437	\$ 466	\$ 496
Other Carrier Revenues	82	91	96		
Total Carrier Services Revenues (1)	\$ 448	\$ 502	\$ 534		
Other Revenues	173	329	371		
<b>Total Revenues</b>	\$ 620	\$ 831	\$ 905 (2)		
<b>Direct Costs</b>					
Carrier Services Direct Costs (1)	\$ 57	\$ 64	\$ 67		
% of Carrier Services Revenues	13%	13%	13%		
Other Direct Costs (1)	95	179	201		
<b>Total Direct Costs</b>	\$ 152	\$ 242	\$ 268		
<b>Segment Contribution</b>					
Carrier Services	\$ 391	\$ 438	\$ 466		
Other	78	151	170		
<b>Total</b>	\$ 469	\$ 589	\$ 636		
<b>Indirect Expenses</b>					
Sales and Marketing	\$ 17	\$ 24	\$ 27		
Estimated Corporate Overhead	25	25	25		
Other Indirect Expenses	157	171	190		
% of Sales	25%	21%	21%		
<b>Total Indirect Expenses</b>	\$ 199	\$ 219	\$ 242		
% of Sales	32%	26%	27%		
<b>EBITDA and EBIT</b>					
EBITDA excl. Non-Recurring Costs and Intangibles Amortization ("Adjusted EBITDA")	\$ 269	\$ 370	\$ 394		
% of Sales	43%	44%	44%		
Depreciation	34	43	44		
% of Sales	5%	5%	5%		
EBIT excl. Non-Recurring Costs and Intangibles Amortization ("Adjusted EBIT")	\$ 235	\$ 327	\$ 350		
% of Sales	38%	39%	39%		
Less: Amortization of Intangibles	12	50	50		
Less: Acquisition-Related Costs	14	-	-		
<b>Reported EBIT</b>	\$ 209	\$ 277	\$ 300 (2)		
<b>Estimated Portion of Adjusted EBITDA and Adjusted EBIT Attributable to NPAC Contract</b>					
<b>Low Estimate (3)</b>					
Revenues	\$ 366	\$ 411	\$ 437	\$ 466	
Less: Allocation of Carrier Service Direct Costs	46	52	55		
% of Revenues	13%	13%	13%		
Less: Allocation of Indirect Costs	118	108	117		
% of Revenues	32%	26%	27%		
<b>Estimated NPAC Contract EBITDA</b>	\$ 202	\$ 250	\$ 265	\$ 282	
% of Revenues	55%	61%	61%	61%	
Less: Allocation of Depreciation	20	21	21		
% of Revenues	5%	5%	5%		
<b>Estimated NPAC Contract EBIT</b>	\$ 182	\$ 229	\$ 244	\$ 260	
% of Sales	50%	56%	56%	56%	
<b>High Estimate</b>					
Revenues	\$ 366	\$ 411	\$ 437	\$ 466	
Less: Allocation of Carrier Service Direct Costs (4)	24	27	29		
% of Revenues	7%	7%	7%		
Less: Allocation of Indirect Costs (5)	93	84	92		
% of Revenues	25%	21%	21%		
<b>Estimated NPAC Contract EBITDA</b>	\$ 249	\$ 299	\$ 317	\$ 337	
% of Revenues	68%	73%	72%	72%	
Less: Allocation of Depreciation	20	21	21		
% of Revenues	5%	5%	5%		
<b>Estimated NPAC Contract EBIT</b>	\$ 229	\$ 278	\$ 295	\$ 314	
% of Sales	63%	68%	68%	68%	

(1) As per segment reporting provided by Neustar

(2) Revenues and EBIT based on midpoint of guidance provided by Neustar on Feb 2013 earnings release; certain expense figures are estimated based on 2012 levels.

(3) Assumes carrier service direct costs are allocated proportional to revenues within carrier service segment, and that all indirect costs and depreciation are allocated proportional to total revenues.

(4) Assumes non-NPAC carrier services revenues generate 60% segment contribution margin.

(5) Assumes all indirect costs and depreciation are allocated proportional to total revenues,

except that sales and marketing costs and estimated \$25mm of corporate overhead are assumed to not be attributable to NPAC contract.