

FCC's Designated Entity Program Reform

**Materials Prepared for the Advisory Committee on Diversity for
Communications in the Digital Age**

April 23, 2006

Disclosure

Council Tree Communications, Inc. (“Council Tree”), of which Steve Hillard is the President, has assisted in the development and organization of minority- and small-business-controlled investment groups that participated in prior Commission auctions as part of the designated entity (“DE”) program. It seeks to assist in the development and organization of one or more minority- or small business-controlled entities that will participate in the Commission’s forthcoming Auction 66 as part of the DE program. Council Tree has participated actively in the Commission proceeding at issue here (WT Docket No. 05-211), urging the Commission to restrict the award of DE benefits where an otherwise qualified DE applicant has any material relationship with an in-region service provider with wireless service revenues that equal or exceed \$5 billion. Council Tree has urged the Commission to complete the adoption of any such new rule in advance of the forthcoming Auction 66. The complete record of that proceeding, including the full text of Council Tree’s various submissions, is available on the Commission’s website.

FCC Spectrum Auctions Primer

The FCC Conducts Auctions of Wireless Spectrum Licenses and Offers Special Advantages to Aid the Participation of Smaller Businesses

- ▶ **In 1993, Congress authorized the FCC to auction licenses to use electromagnetic spectrum under Section 309(j) of the Communications Act**
 - Over 50 FCC auctions that have raised billions of dollars for the Treasury

- ▶ **Section 309(j) directs the FCC to ensure that small businesses, rural telcos, and businesses owned by members of minority groups and women have the opportunity to meaningfully participate in the provision of spectrum-based services**
 - FCC assists these “Designated Entities” (DEs) in its spectrum auctions through various mechanisms
 - Examples: DEs get bid credits (typically 25%) in order to compete against vastly larger, deep-pocketed carriers
 - With loss of tax certificate program, this is the only remaining tool the FCC has that has real economic leverage to foster diversity of ownership in communications

- ▶ **Upcoming Advanced Wireless Services (“AWS”) Auction will bring an estimated \$15+ Billion of proceeds to the US Treasury**
 - Scheduled to begin June 29th; short form applications due May 10th
 - Largest-ever auction, with 90 MHz of spectrum nationwide

The Issue

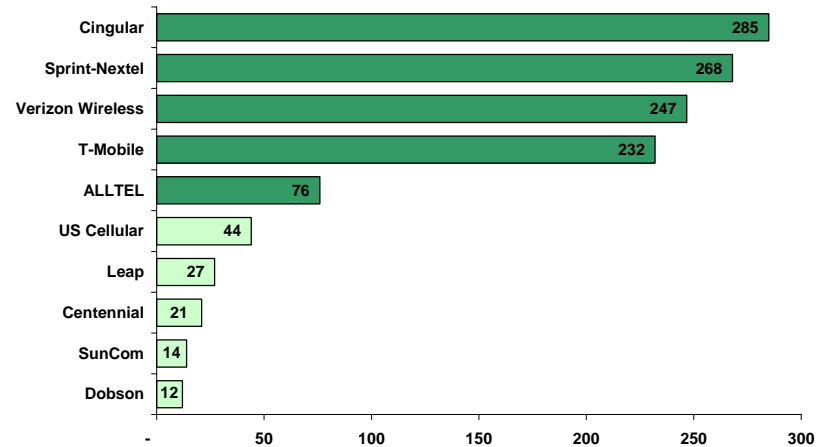
A clear trend has emerged in recent auctions, with the national wireless carriers (i.e. those with nationwide footprints) using the DE program to extend their already considerable industry influence. This pattern may jeopardize the entire DE program.

- ▶ **The top-5 national wireless carriers already dominate the wireless industry**
 - Top-5 control roughly 90% of wireless industry subscribers and spectrum
 - ▶ **The national carriers have been actively using these DE partnerships, as demonstrated in the recent Auction 58 in January of 2005**
 - \$2 billion FCC auction of wireless license
 - National carriers used DEs to acquire 71% of their spectrum
 - Only 29% of their spectrum acquired directly by national carriers
 - ▶ **DEs need access to sources of capital and expertise, but the benefits of that policy are outweighed when already-dominant national carriers are the source**
 - Serves only to extend industry consolidation and dampen new competition
 - National carriers have zero need of government assistance
 - ▶ **In the Further Notice of Proposed Rulemaking (“FNPRM”), the Commission unanimously adopted a tentative conclusion to withhold DE benefits where DEs had relationships with large, in-region wireless carriers**
 - Focusing on the top-5 national wireless carriers
 - ▶ **This is an important matter within the mandate of the Diversity Advisory Committee to advise the Commission**
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National Carrier Metrics

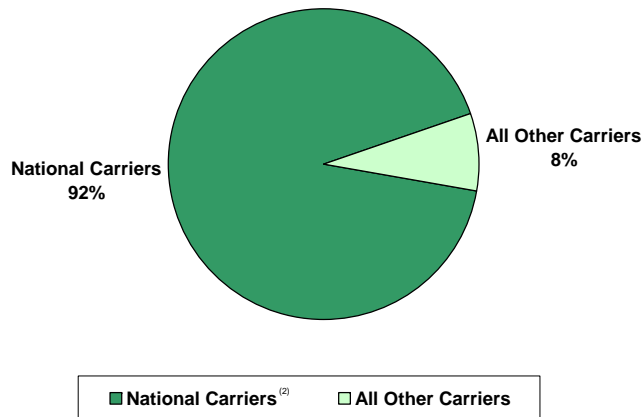
▶ A solid record of data demonstrates national carrier dominance of the industry

Top-10 Public Wireless Carriers -- Covered POPs⁽¹⁾
(in millions)

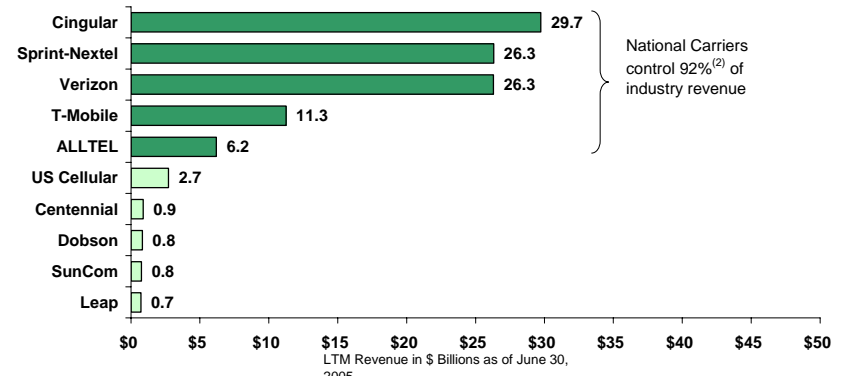


(1) Source: As publicly available from Company Reports, Bear Stearns "US Wireless Industry -- January 2006", Lehman Brothers Equity Research -- "Leap Wireless International, January 23, 2006" -- does not include data on private companies such as MetroPCS

U.S. Wireless Industry Service Revenue⁽¹⁾



Top-10 Public Wireless Carriers - Service Revenue⁽¹⁾
(in \$ billions)



(1) Last Twelve Months as of June 30, 2005. Total industry LTM revenue of \$108.5 billion based on CTIA's Semi-Annual Wireless Industry Survey for June 2005

(2) Carrier revenue based on SEC filings and company reports. National Carriers defined as Cingular, Sprint, Verizon Wireless,

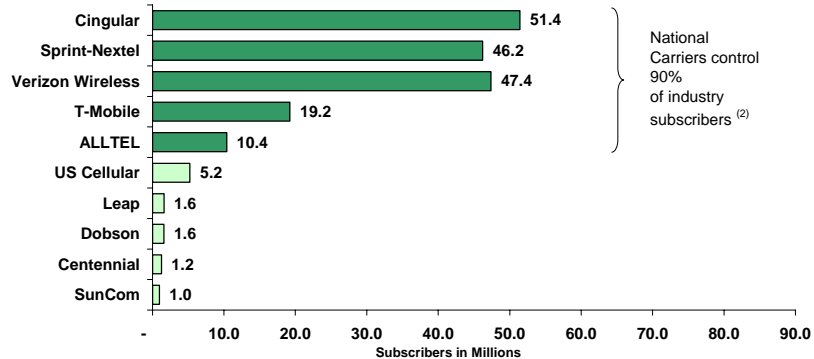
(1) Carrier revenue based on SEC filings and company reports. National Carriers defined as Cingular, Sprint, Verizon Wireless, T-Mobile and Alltel. Does not include private companies such as MetroPCS

(2) Total industry LTM revenue of \$108.5 billion based on CTIA's Semi-Annual Wireless Industry Survey for June 2005

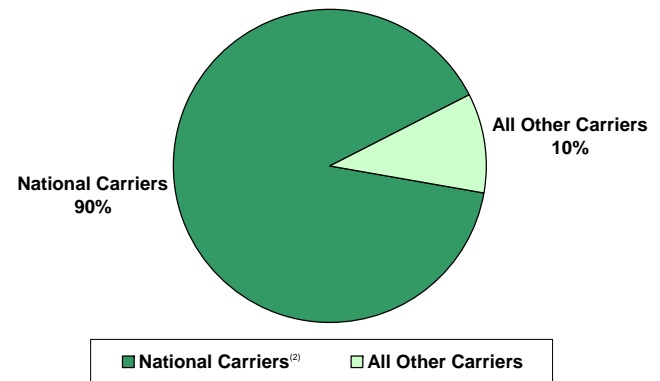
National Carrier Metrics (cont'd)

Additional data further underscores industry concentration

Top-10 Public Wireless Carriers Subscribers ⁽¹⁾
(in millions)



U.S. Wireless Industry Subscribers ⁽¹⁾



⁽¹⁾ As of June 30, 2005. Carrier subscribers based on SEC filings and company reports. National Carriers defined as Cingular, Sprint and its affiliates, Verizon Wireless, T-Mobile and Alltel. Does not include private companies such as MetroPCS

⁽²⁾ Total industry subscribers of 194.5 million based on CTIA's Semi-Annual Wireless Industry Survey for June 2005

⁽¹⁾ As of June 30, 2005. Total industry subscribers of 194.5 million based on CTIA's Semi-Annual Wireless Industry Survey for June 2005

⁽²⁾ Carrier subscribers based on SEC filings and company reports. National Carriers defined as Cingular, Sprint and its affiliates, Verizon Wireless, T-Mobile and Alltel

Recent PCS Auction Results

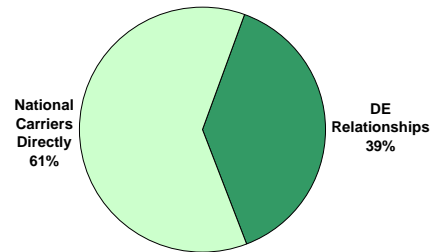
The problem is underscored by data clearly showing that national wireless carriers increasingly use DE investments to access additional CMRS spectrum

How National Carriers Amass Spectrum

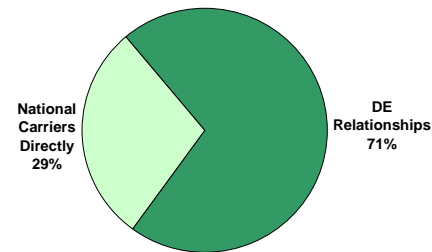
(Directly or via DE Relationships)

Measured by:
**Net License
Purchase Price**

Auction 35 (Jan 2001)

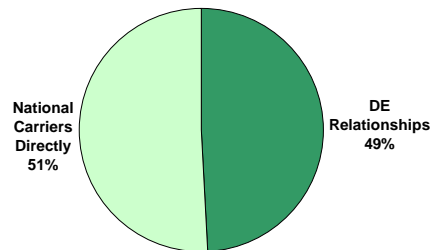


Auction 58 (Feb 2005)

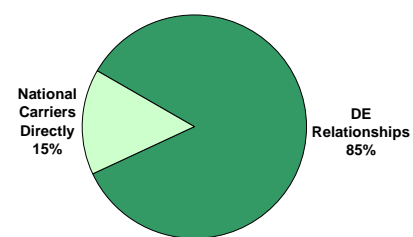


Measured by:
By MHz-POPs

Auction 35 (Jan 2001)



Auction 58 (Feb 2005)

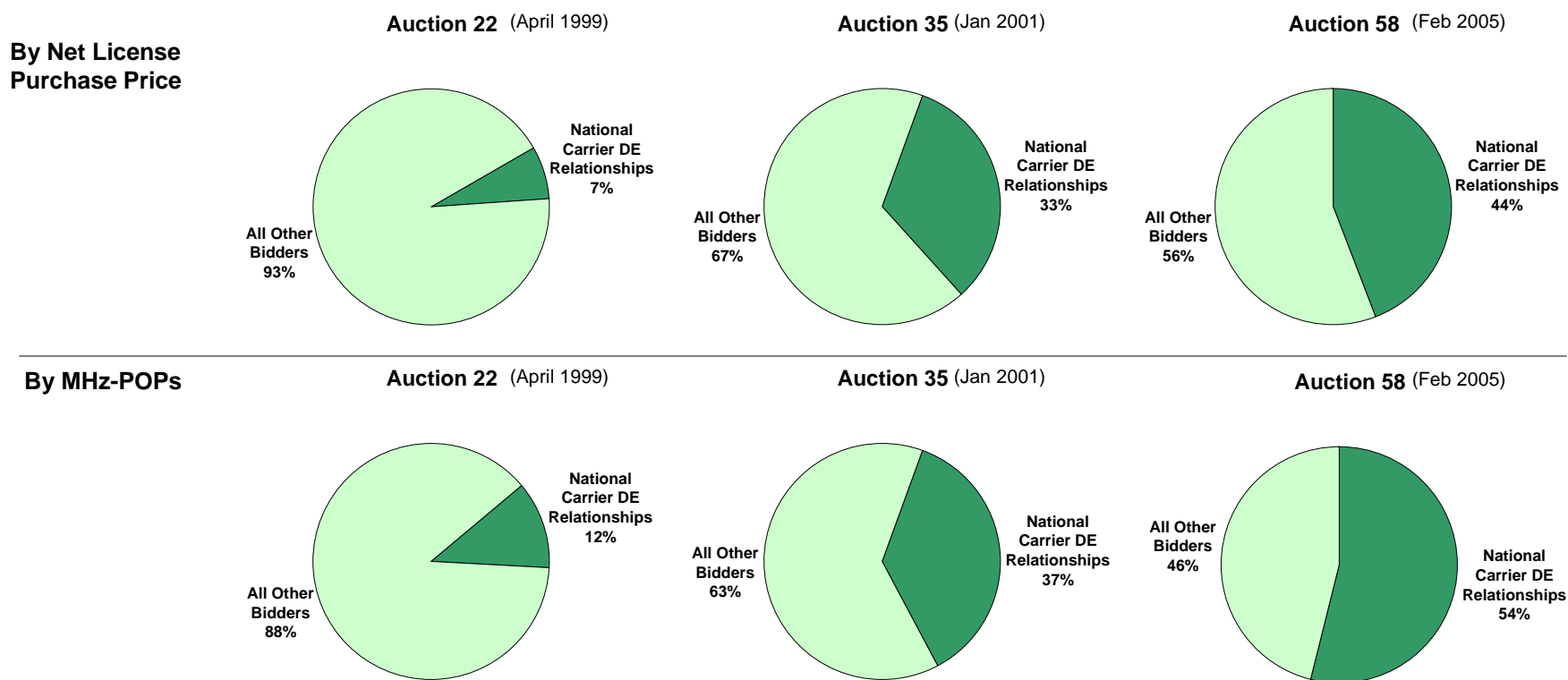


(1) National carrier DEs include: Vista PCS (Verizon), Cook Inlet/VS GSM VII PCS (T-Mobile), Edge Mobile (Cingular) and Wirefree Partners III (Sprint).

Recent PCS Auction Results (continued)

The problem is further underscored by data clearly showing that DEs associated with national carriers win very large and growing shares of CMRS auction licenses

Spectrum Won by DEs with National Carrier Relationships



► **An accelerating trend with clear implications for Auction 66**

The Solution

The FCC released a FNPRM with a unanimous Tentative Conclusion to restrict the award of DE benefits where a DE has a material relationship with a large, in-region wireless service provider

- ▶ **The FCC released the FNPRM on February 3, 2006**
 - Public comments and reply comments completed March 3rd
 - FCC final decision pending / imminent
- ▶ **The FNPRM sought comment on the proposal to define large carriers as those with wireless revenues of > \$5 billion, which would encompass the top-5 national carriers**
 - The Tentative Conclusion would prohibit the award of bidding credits or other small business benefits to entities that have “material relationships” with a “large in-region incumbent wireless service provider”
- ▶ **Adoption of the tentative conclusion would allow DEs the opportunity to more effectively compete with entrenched national wireless carriers if other sources of capital and expertise are preserved**
- ▶ **The FCC’s final decision on this matter is pending / imminent**
 - Must happen quickly to avoid AWS-auction delay and further prejudice to DE opportunities

Proceeding Status

The Tentative Conclusion was supported by the vast majority of commenters

- ▶ **The Commission has before it a powerful record to support its Tentative Conclusion to limit national wireless carrier partnerships with DEs**
 - 35 Comments representing 46 parties (only 5 opposed)
 - 17 Reply Comments representing 60 parties (only 5 opposed)
 - The Department of Justice supported the Tentative Conclusion
 - The Congressional Black Caucus supported the Tentative Conclusion

- ▶ **Supporters include a diverse array of groups**
 - DEs, rural telcos, consumer groups, minority groups, small & regional wireless carriers and private equity investors

- ▶ **Opposition came predictably from CTIA, three of the five large national carriers, and two of their DEs**
 - CTIA, Verizon Wireless, Cingular (filed reply comments only), T-Mobile
 - Cook Inlet (a DE associated with T-Mobile) and Wirefree Partners (a DE associated with Sprint)

Proposed Action by the DAC

- ▶ **The \$5 billion wireless revenue threshold is the right cutoff for defining large national carrier and restricting the award of DE benefits**
 - Fully supported by the record
 - The only demonstrated problem in the record of this proceeding is with national wireless carriers
 - The Commission apparently has considered extending the limitation to the bottom 10% of carriers or to non-wireless communications companies, but doing so is wrong and has no support in the record of this proceeding

- ▶ **DEs must be able to secure capital and expertise from smaller and mid-sized wireless carriers to attract investment from other sources, to compete against national carriers at auction, and to construct and operate competitive wireless networks**

- ▶ **Proposed Action by the Diversity Advisory Committee:**
 - **Adoption of the attached Draft resolution**
 - **Confirm these three points to the Commission**
 - DE program has been a success story
 - The DE program, like any government program, must be re-tuned from time to time to keep pace with industry change
 - Adoption of a limitation affecting investments by the bottom 10% of wireless carriers (i.e., those other than the top-5 who control 90% of the market) or to non-wireless communications companies would undermine the DE program

Resolution Regarding Designated Entity Investment Rules

WHEREAS, the Commission's Designated Entity ("DE") rules were developed to satisfy the Commission's obligations under Section 309(j) of the Communications Act to avoid the excessive concentration of licenses and provide small businesses and businesses owned by members of minority groups and women (collectively, "DEs") with the meaningful opportunity to participate in the provision of spectrum-based services;

WHEREAS, the often times capital-intensive nature of communications businesses and the difficulties experienced by DEs in accessing capital and experience make it virtually impossible for DEs to secure valuable spectrum licenses when bidding against well-capitalized incumbents and to compete in the market;

WHEREAS, the Commission's DE rules have consistently been designed to ensure that DEs who participate in competitive bidding have sufficient capital and flexibility to structure their businesses to be able to compete at auction, fulfill their payment obligations, and ultimately provide service to the public;

WHEREAS, in a proceeding captioned WT Docket No. 05-211 ("Proceeding"), the Commission is currently considering whether to modify its DE rules to prohibit the award of competitive bidding preferences to DEs having material relationships with large in-region incumbent wireless services providers; and

WHEREAS, it appears that, as part of the Proceeding, the Commission is considering the adoption of a much broader rule, including one that would prohibit the award of competitive bidding preferences to DEs having material investment from or relationships with any entity with revenues in excess of \$125 million or one that would prohibit the award of competitive bidding preferences to DEs having material investment from or relationships with any large non-wireless service communications provider;

Therefore, be it

RESOLVED that the Advisory Committee on Diversity for Communications in the Digital Age strongly urges the Commission not to adopt a much broader rule that would prohibit the award of competitive bidding preferences to DEs having material investment from or relationships with any entity with revenues in excess of \$125 million or with any large non-wireless service communications provider. The Commission should not extend any such prohibition beyond the largest national wireless carriers. The wireless industry is extremely capital-intensive and technically complex. DEs must have access to sources of capital and expertise to have any chance of acquiring licenses and successfully providing service. Limiting DE relationships when they do not involve the largest national wireless carriers would have the effect of depriving DEs of their most logical sources of investment and experience. This would be inconsistent with the directives of Section 309(j), with many years of Commission precedent, and with the Commission's desire to promote diversity in the ranks of its licensees.

FURTHER RESOLVED the Commission should adopt the Tentative Conclusion and prohibit the award of preferences to DEs having material relationships with large in-region incumbent wireless services providers that have wireless revenues at \$5 billion or more.



**Congress of the United States
House of Representatives**

March 3, 2006

The Honorable Kevin J. Martin
Chairman
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

RE: WT Docket No. 05-211

Dear Chairman Martin:

As members of the Congressional Black Caucus, we would like to express our concern regarding the unprecedented consolidation of ownership taking place in the United States wireless service industry and its impact on small businesses and businesses owned by members of minority groups and women. As we look forward to the Advanced Wireless Services auction, we are concerned about ensuring the effectiveness of the Designated Entity (DE) Program and seeing that it accomplishes the intent of Congress in giving the Commission authority to award licenses by competitive bidding.

The DE Program is a product of Congress' instruction that the Commission ensure that small businesses and businesses owned by members of minority groups and women have a meaningful opportunity to participate in the provision of spectrum-based services. Congress also directed the Commission to conduct competitive bidding in a way designed to avoid the excessive concentration of licenses. In the face of ongoing wireless industry consolidation and waning minority ownership and participation in the communications industry, it is now more important than ever to ensure that the DE Program serves its original purposes.

We are concerned that the Commission's current auction rules, well-intended though they may have been, allow large national carriers to extend their already-considerable influence in the industry through material partnerships with DEs. It is important that DEs have sources of capital and industry experience on which to rely, but allowing national wireless carriers to perform these functions is no longer good policy in light of their overwhelming dominance in the industry. The result is that most DEs – smaller businesses, new entrants, and minority and women-owned businesses – are hampered in their ability to compete effectively in the auctions and in post-auction markets against the large national carriers and their partners.

We urge the Commission to adopt the fundamental changes to the DE Program outlined in the Further Notice for Proposed Rulemaking dated February 3, 2006 to address this situation. Specifically, we recommend rules to prohibit the award of bidding credits or other small business benefits to entities that are partnered with the five largest national wireless service providers. In doing so, the Commission should also ensure that small businesses have access to both capital

The Honorable Kevin J. Martin

3/3/2006

Page 2 of 3

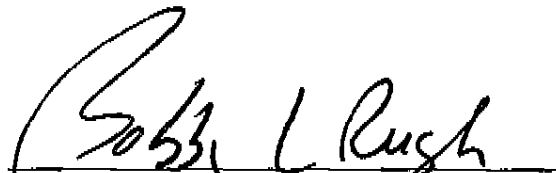
and expertise from all other sources of capital – including other telecommunications companies – in order to build competitive wireless networks.

These changes to the DE Program will help promote competition and diversity of ownership in the wireless industry, benefiting carriers and consumers alike. We must continue to provide mechanisms that offer incentives and resources for small enterprises and businesses owned by members of minority groups and women to participate in the provision of spectrum-based services to consumers in rural, urban, and under-served areas. We urge the Commission to implement the changes outlined in this letter.

Sincerely,



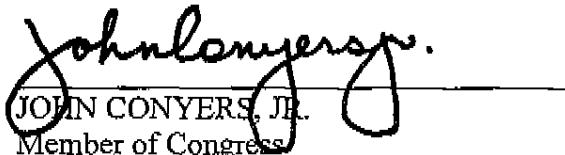
DIANE E. WATSON
Member of Congress



BOBBY L. RUSH
Member of Congress



WILLIAM JEFFERSON
Member of Congress



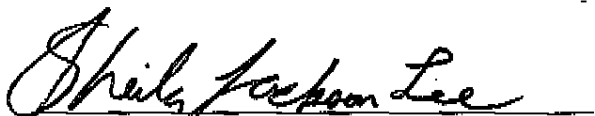
JOHN CONYERS, JR.
Member of Congress



EDOLPHUS TOWNS
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MAJOR R. OWENS
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SHEILA JACKSON-LEE
Member of Congress



CHARLES B. RANGEL
Member of Congress


The Honorable Kevin J. Martin

3/3/2006

Page 3 of 3



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