Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Commercial Spectrum	)	
Enhancement Act and Modernization of the	)	WT Docket No. 05-211
Commission's Competitive Bidding Rules and	)	
Procedures	)	

SECOND REPORT AND ORDER

AND SECOND FURTHER NOTICE OF PROPOSED RULE MAKING

Adopted: April 25, 2006 **Released: April 25, 2006**

Comment Date: 60 days after publication in the Federal Register
Reply Comment Date: 90 days after publication in the Federal Register

By the Commission: Chairman Martin and Commissioner Copps issuing separate statements; and Commissioner Adelstein approving in part, dissenting in part, and issuing a separate statement.

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I. INTRODUCTION

1. In this *Second Report and Order* and *Second Further Notice of Proposed Rule Making* ("*Second Further Notice*"), we address our rules concerning the eligibility of applicants and licensees for designated entity benefits. In the *Second Report and Order*, we modify our rules in order to increase our ability to ensure that the recipients of designated entity benefits are limited to those entities and for those purposes Congress intended.[1] In the *Second Further Notice*, we seek comment on a variety of additional measures that might further augment the effectiveness of our rules in this regard. We take all of these steps with the goal of enhancing our ability to carry out Congress's dual directives with regard to designated entities: (1) that we ensure that designated entities are given the opportunity to participate in the provision of spectrum-based services;[2] and (2) that, in providing such opportunity, we prevent unjust enrichment.[3] With regard to the second directive, our particular intention is to ensure that entities ineligible for designated entity incentives cannot circumvent our rules by obtaining those benefits indirectly, through their relationships with eligible entities.

2. In the *Further Notice of Proposed Rule Making* in this docket ("*Further Notice*"), we tentatively concluded that we should restrict the award of designated entity benefits to an otherwise qualified applicant where it has a "material relationship" with a "large in-region incumbent wireless service provider."[4] We sought comment on how we should define the elements of such a restriction.[5] We further sought comment on whether we should restrict the award of designated entity benefits where an otherwise qualified applicant has a "material relationship" with a large entity that has a significant interest in communications services, and if so, how we should define the elements of such a restriction.[6]

A. *Second Report and Order*

3. As discussed fully below, we revise our general competitive bidding rules ("Part 1" rules)[7] governing benefits reserved for designated entities[8] to include certain "material relationships" as

[1] "Designated entities" are small businesses, businesses owned by members of minority groups and/or women, and rural telephone companies. 47 C.F.R. § 1.2110(a). In an effort to eliminate some past inconsistency in nomenclature, we clarify that, unless otherwise noted, when referring to "designated entities," we include as a subgroup "entrepreneurs" eligible to bid for "set-aside" broadband Personal Communications Service ("broadband PCS") licenses offered in closed bidding. *See id.* §§ 1.2110(a), 24.709.

[2] 47 U.S.C. § 309(j)(4)(D); *see also id.* § 309(j)(3)(B).

[3] *Id*. § 309(j)(4)(E); *see also id.* § 309(j)(3)(C).

[4] Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, WT Docket No. 05-211, *Further Notice of Proposed Rule Making*, 21 FCC Rcd 1753 (2006) ("*Further Notice*").

[5] *Id*. at 1754-55 ¶ 1.

[6] *Id.* In response, we received 37 comments and 18 reply comments. Two parties who filed initial comments in response to the Commission's Public Notice relating to AWS auction procedures (AU-06-30) also raised issues with respect to the Commission's designated entity program. We also received *ex parte* filings in response to the *Further Notice* from various parties including the Congressional Black Caucus, the U.S. Department of Justice and Council Tree. Appendix A contains a list of full and abbreviated names of commenting parties.

[7] *See* 47 C.F.R. § 1.2101 *et. seq*.

[8] *See id.* § 1.2110. The Commission establishes special small business size standards on a service-specific basis, (continued....)

factors in determining designated entity eligibility. Specifically, we adopt rules to limit the award of designated entity benefits, as explained in more detail below, to any applicant or licensee that has "impermissible material relationships" or an "attributable material relationship" created by certain agreements with one or more other entities for the lease or resale (including under a wholesale arrangement) of its spectrum capacity. These definitions of material relationships are necessary to strengthen our implementation of Congress's directives with regard to designated entities and to ensure that, in accordance with the intent of Congress, every recipient of our designated entity benefits is an entity that uses its licenses to directly provide facilities-based telecommunications services for the benefit of the public.[9]

4. We also adopt rule modifications to strengthen our unjust enrichment rules so as to better deter entities from attempting to circumvent our designated entity eligibility requirements and to recapture designated entity benefits when ineligible entities control designated entity licenses or exert impermissible influence over a designated entity.[10] Similarly, to ensure our continued ability to safeguard the award of designated entity benefits, we provide clarification regarding how the Commission will implement its rules concerning audits, and we refine our rules with respect to the reporting obligations of designated entities.

5. The rules we adopt today will apply to all determinations of eligibility for all designated entity benefits, including bidding credits and, as applicable, set-asides[11] and installment payments, unless

(...continued from previous page)
taking into consideration the characteristics and capital requirements of the particular service. 47 C.F.R. §1.2110(c)(1). In the *Part 1 Fifth Report and Order,* the Commission, in light of the *Adarand* decision, declined to adopt special provisions for minority- and women-owned businesses but noted that minority- and women-owned businesses that qualify as small businesses may take advantage of the provisions the Commission has adopted for small businesses. Amendment of Part 1 of the Commission's Rules – Competitive Bidding Procedures, WT Docket No. 97-82, *Order on Reconsideration of the Third Report and Order, Fifth Report and Order, and Fourth Further Notice of Proposed Rule Making*, 15 FCC Rcd 15293, 15319 ¶ 48 (2000) ("*Part 1 Fifth Report and Order*") (citing *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200, 227 (1995)). On several occasions, the Commission has declined to adopt bidding credits for large telephone companies that serve rural areas. *See, e.g.*, Implementation of Section 309(j) of the Communications Act – Competitive Bidding, PP Docket No. 93-253, *Fifth Memorandum Opinion and Order*, 10 FCC Rcd 403, 457-58, 462-63 ¶¶ 100, 111 (1994) ("*Competitive Bidding Fifth MO&O*"); Amendment of Part 1 of the Commission's Rules – Competitive Bidding Procedures, *Order on Reconsideration of the Third Report and Order, Fifth Report and Order, and Fourth Notice of Proposed Rule Making,* 15 FCC Rcd 15293, 15320-21 ¶¶ 51-52 (2000); Reallocation and Service Rules for the 698-746 MHz Spectrum Band (Television Channels 52-59), GN Docket No. 01-74, *Report and Order*, 17 FCC Rcd 1022, 1090-91 ¶ 176 (2002). The Commission determines eligibility for its small business provisions based on an entity's size determined pursuant to attribution rules. 47 C.F.R. § 1.2110(b)(1)-(3). *But see* Amendment of Part 1 of the Commission's Rules – Competitive Bidding Procedures, *Second Order on Reconsideration of the Third Report and Order and Order on Reconsideration of the Fifth Report and Order*, 18 FCC Rcd 10180, 10191-94 ¶¶ 16-18 (2003) (establishing exemption for rural telephone cooperatives from the requirement that gross revenues of entities controlled by an applicant's officers and directors be attributed to the applicant), *modified on reconsideration, Second Order on Reconsideration of the Fifth Report and Order*, 20 FCC Rcd 1942 (2005); 47 C.F.R. § 1.2110(b)(3)(iii) (exempting rural telephone cooperatives from attributing the gross revenues of its officers and directors).

[9] In the legislative history of Section 309(j), Congress explains that the reason for imposing anti-trafficking restrictions and unjust enrichment payment obligations on entities that receive small business benefits is to deter "participation in the licensing process by those who have no intention of offering service to the public." H.R. REP. NO. 103-111, at 257-58 (1993) (Conference Agreement adopted House provisions, in relevant part, with amendments. H.R. CONF. REP. NO. 103-213, at 483 (1993)).

[10] *See* 47 C.F.R. § 1.2111.

[11] Broadband Personal Communications Services entrepreneurs will be subject to these new rules as described below.

excepted by the grandfathering provisions described in detail below.[12] These rules will be applied to any application filed to participate in auctions in which bidding begins after the effective date of the rules adopted herein and to all long-form applications filed by winning bidders after such auctions,[13] as well as to all applications for an authorization, an assignment or transfer of control, a lease, or reports of events affecting a designated entity's ongoing eligibility,[14] including "impermissible material relationships" or "attributable material relationships," filed on or after release of this *Second Report and Order*. These rules will become effective thirty days after their publication in the Federal Register.

B. *Second Further Notice of Proposed Rule Making*

6. In reviewing the record in this proceeding, including the requests of various parties to conduct a further inquiry,[15] we issue this *Second Further Notice* to consider whether we should adopt additional restrictions, beyond those we adopt herein, to further safeguard the benefits reserved for designated entities.[16]

II. BACKGROUND

7. Throughout the history of the auctions program, the Commission has endeavored to carry out its Congressional directive to promote the involvement of designated entities in the provision of spectrum-based services.[17] Congress recommended that the Commission, in assisting designated entities, consider the use of various mechanisms such as tax credits and bidding preferences.[18] Yet, in so doing, Congress also mandated that the Commission safeguard the award of the benefits it distributed to "prevent unjust enrichment as a result of the methods employed to issue licenses."[19]

8. The challenge for the Commission in carrying out Congress's plan has always been to find a reasonable balance between the competing goals of, first, providing designated entities with reasonable flexibility in being able to obtain needed financing from investors and, second, ensuring that the rules effectively prevent entities ineligible for designated entity benefits from circumventing the intent of the rules by obtaining those benefits indirectly, through their investments in qualified businesses.[20] The changes in the Commission's designated entity rules over time have been the result of the Commission's continuing effort to maintain this balance effectively in the face of a rapidly evolving telecommunications industry, legislative changes, judicial decisions, and the demand of the public for greater access to wireless services.

9. The Commission's primary method of promoting the participation of designated entities in competitive bidding has been to award bidding credits – percentage discounts on winning bid amounts

[12] *See* discussion *infra* ¶¶ 28-30.

[13] The rules adopted herein, therefore, will not apply to the upcoming auction of 800 MHz Air-Ground Radiotelephone Service licenses, scheduled to begin on May 10, 2006, nor to the Form 601 applications to be filed subsequent to the close of that auction by the winning bidders. *See* Auction of 800 MHz Air-Ground Radiotelephone Service Licenses Scheduled for May 10, 2006; Notice and Filing Requirements, Minimum Opening Bids, Upfront Payments and Other Procedures for Auction No. 65, *Public Notice*, 21 FCC Rcd 1278 (2006).

[14] *See* discussion *infra* note 116 and accompanying text.

[15] *See, e.g.*, Comments of NHMC at 17-18; Reply Comments of Consumers Union at 1-2.

[16] *See supra* note 8 (discussing the Commission's designated entity benefits).

[17] *See* 47 U.S.C. § 309(j)(4)(D); *see also* 47 C.F.R. § 1.2110(a).

[18] 47 U.S.C. § 309(j)(4)(D).

[19] *Id*. § 309(j)(4)(E).

[20] *See* Implementation of Section 309(j) of the Communications Act - Competitive Bidding, PP Docket No. 93-253, *Fifth Report and Order*, 9 FCC Rcd 5532, 5582 ¶ 159 (1994) ("*Competitive Bidding Fifth Report and Order*").

– to small business applicants.[21] The Commission also has utilized other incentives, such as installment payments and, in the broadband Personal Communications Services ("broadband PCS"), a license set-aside, to encourage designated entities to participate in spectrum auctions and in the provision of service.[22] In order to qualify for these benefits, an applicant must demonstrate that its gross revenues (and, in some cases, its total assets), in combination with those of its "attributable" interest holders, fall below certain service-specific financial caps.[23] Thus, in determining eligibility for size-based benefits, it is critical to decide which investors' gross revenues (and total assets) must be attributed.

10. During the early years of the designated entity program, the Commission adopted often complicated attribution rules on a service-specific basis. For broadband PCS attribution, the Commission had a "general rule" – its financial caps[24] – and four exceptions to the rule.[25] Two of these exceptions came to be known as the "control group exceptions" – a 25 percent equity exception and a 49.9 percent equity exception.[26] Both exceptions required the applicant to form a "control group"[27] within which "qualifying investors"[28] owned at least 50.1 percent of the applicant's voting interests.[29] Under the 25 percent equity exception, the applicant's control group was required to own at least 25 percent of the applicant's total equity; and, within the control group, qualifying investors were required to hold at least 15 percent of the applicant's total equity.[30] Under the 49.9 percent equity exception, the applicant's control group was required to own at least 50.1 percent of the applicant's total equity; and, within the control group, qualifying investors were required to hold at least 30 percent of the applicant's total equity.[31] If these and certain other requirements were met, the gross revenues and total assets of non-controlling investors were not attributed to the applicant.[32] These two exceptions to the general rule were widely used; however, the other two exceptions – one for publicly-traded corporations with widely dispersed voting stock ownership and the other for small business consortia[33] – were seldom invoked.

11. The Commission used the control group approach in broadband PCS for determinations of small business eligibility and also for determinations of "entrepreneur" eligibility. In broadband PCS,

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[21] *See, e.g.,* Implementation of Section 309(j) of the Communications Act – Competitive Bidding, PP Docket No. 93-253, *Second Report and Order*, 9 FCC Rcd 2348, 2391-92 ¶¶ 241-44 (1994) ("*Competitive Bidding Second Report and Order*").

[22] *See id.* at 2389-91, 2392 ¶¶ 231-40, 245-48.

[23] *See* 47 C.F.R. § 1.2110(b).

[24] *See id.* § 24.709(a)(1)-(2).

[25] *See id.* § 24.709(b)(1)(i)-(iv).

[26] *See id.* § 24.709(b)(1)(iii), (iv).

[27] A control group is an entity, or a group of individuals or entities, that possesses *de jure* and *de facto* control of an applicant or licensee. *See id*. § 24.720(k).

[28] A qualifying investor is a person who is (or holds an interest in) a member of the applicant's control group and whose gross revenues and total assets, when aggregated with those of all other attributable investors and affiliates, do not exceed the entrepreneurs' block gross revenues and total assets limits. *Id.* § 24.720(n).

[29] *Id.* § 24.709(b)(1)(v)(A)(2), (b)(1)(vi)(A)(2). If the applicant was a partnership, the control group was required to hold all of its general partnership interests. *Id.*

[30] *Id.* § 24.709(b)(1)(v)(A), (b)(1)(v)(A)(1).

[31] *Id.* § 24.709(b)(1)(vi)(A), (b)(1)(vi)(A)(1).

[32] *Id.* § 24.709(b)(1)(iii)-(vi). The equity ownership requirements under both exceptions were somewhat relaxed for entities that had been operating and earning revenues for at least two years prior to December 31, 1994. *Id.* §§ 24.709 (b)(1)(v)(B), 24.709(b)(1)(vi)(B), 24.709(b)(6)(ii), 24.720(h).

[33] *See id.* § 24.709(b)(i), (ii).

the Commission originally "set aside" C and F block licenses for "entrepreneurs,"[34] small entities whose gross revenues and total assets, when aggregated with those of their attributable interest holders, fell below certain financial caps.[35] A variation of this control group approach was employed for narrowband PCS.[36] In determining whether applicants for the 900 MHz specialized mobile radio ("SMR") service qualified as small businesses, the Commission attributed the revenues of parties holding partnership and other ownership interests and any stock interest amounting to 20 percent or more of the equity, or outstanding stock, or outstanding voting stock of the applicant.[37] For virtually all other services, the Commission used a "controlling interest"[38] or "controlling principal"[39] standard much like the attribution standard used today. Under this earlier standard, the Commission attributed to the applicant the gross revenues of its controlling interests and their affiliates in assessing whether the applicant was qualified to take advantage of the Commission's small business provisions, such as bidding credits.[40]

12. Since 2000, the Commission has applied the current "controlling interest" standard to all services when making attribution determinations.[41] Under this standard, the Commission attributes to an applicant the gross revenues of it, its controlling interests, its affiliates, and the affiliates of the applicant's controlling interests.[42] A "controlling interest" includes individuals or entities, or groups of individuals or entities, that have control of the applicant under the principles of either *de jure* or *de facto* control.[43] *De jure* control is typically evidenced by the holding of greater than 50 percent of the voting stock of a corporation or, in the case of a partnership, general partnership interests.[44] *De facto* control is determined on a case-by-case basis[45] and includes the criteria set forth in *Ellis Thompson*.[46] Under the controlling

[34] In some non-PCS services, the Commission uses the term "entrepreneur" to refer to a level of small business eligibility for bidding credits. *See*, *e.g.*, *id.* §§ 22.229, 27.702, 101.538, 101.1107, 101.1112, 101.1429.

[35] In the context of Broadband PCS, an applicant or licensee generally qualifies as an entrepreneur if it, together with its affiliates, persons or entities that hold interests in the applicant or licensee, and their affiliates, has combined total assets of less than $500 million and has had combined gross revenues of less than $125 million in each of the last two years. *Id.* § 24.709(a)(1).

[36] Under this standard, the gross revenues and affiliations of an investor in the applicant were not considered so long as the investor held 25 percent or less of the applicant's passive equity and was not a member of the applicant's control group. Amendment of Part 1 of the Commission's Rules — Competitive Bidding Proceeding, WT Docket 97-60, *Order, Memorandum Opinion and Order, and Notice of Proposed Rule Making*, 12 FCC Rcd 5686, 5702 ¶ 26 (1997) ("*Part 1 Order*").

[37] 47 C.F.R. § 90.814(g) (2001); *see Part 1 Order*, 12 FCC Rcd at 5703 ¶ 27.

[38] *See*, *e.g.*, 47 C.F.R. §§ 1.948, 1.2105, 1.2110, 1.2112, 20.6, 21.38, 22.223, 22.225.

[39] *See*, *e.g.*, *id.* §§ 1.2110, 22.223, 27.210, 90.814, 90.912, 90.1021, 101.1109.

[40] *See Part 1 Order*, 12 FCC Rcd at 5703 ¶ 27.

[41] *See generally Part 1 Fifth Report and Order*, 15 FCC Rcd at 15293.

[42] *Id.* at 15323 ¶ 59.

[43] 47 C.F.R. § 1.2110(c)(2).

[44] *Id*.

[45] *Id.*

[46] In *Ellis Thompson*, the Commission identified the following factors used to determine control of a business: (1) use of facilities and equipment; (2) control of day-to-day operations; (3) control of policy decisions; (4) personnel responsibilities; (5) control of financial obligations; and (6) receipt of monies and profits. Application of Ellis Thompson Corporation, *Memorandum Opinion and Order and Hearing Designation Order*, 9 FCC Rcd 7138, 7138-7139 ¶ 9 (1994) (citing the Commission's decision in *Intermountain Microwave*, Applications for Microwave Transfers to Teleprompter Approved with Warning, *Public Notice*, 12 FCC 2d 559 (1963) ("*Intermountain Microwave*") (1963)). *See also* Application of Baker Creek Communications, L.P. for Authority to Construct and Operate Local Multipoint Distribution Services in Multiple Basic Trading Areas, *Memorandum Opinion and Order*, (continued....)

interest standard, the officers and directors of any applicant are considered to have a controlling interest in the applicant.[47] The Commission has declined to impose minimum equity requirements on controlling interests, believing that such requirements would dictate that a person or entity identified as a controlling interest must retain some level of equity in the applicant, thereby reducing the amount of equity the applicant could offer to non-controlling interests in exchange for financing and making it more difficult for the applicant to attract sufficient investment to compete in the marketplace.[48]

13. In applying the controlling interest standard, the Commission's intent has been to provide designated entities with increased flexibility and simplicity in structuring their businesses, while continuing to ensure that size-based benefits are reserved solely for qualified entities. In making the change, the Commission acknowledged the complexity of the broadband PCS control group approach, emphasizing that the controlling interest standard would be "simpler" and "more straightforward to implement."[49] Also, the Commission explained, application of the controlling interest standard would allow "legitimate small businesses . . . to attract passive financing in a highly competitive and evolving telecommunications marketplace,"[50] while ensuring "that only those entities truly meriting small business status qualif[ied] for [the Commission's] small business provisions."[51]

III. SECOND REPORT AND ORDER

A. Background

14. In the *Further Notice*, we tentatively concluded that we should restrict the award of designated entity benefits to an otherwise qualified applicant where it has a "material relationship" with a "large in-region incumbent wireless service provider."[52] We sought comment on how to define the specific elements of such a restriction.[53] Further, we sought comment on whether such a restriction on the award of designated entity benefits should apply where a designated entity applicant has a "material relationship" with a large entity that has a "significant interest in communication services," and whether we should include in such a definition a broad category of communications-related businesses or instead exclude or include certain types of entities.[54] In addition, we sought comment on whether we should adopt unjust enrichment provisions that would require reimbursement of designated entity benefits in the event that a designated entity makes a change in its material relationships or makes any other changes that would result in the loss of or change in its eligibility subsequent to acquiring a license with a designated

(...continued from previous page)
13 FCC Rcd 18709 (Wireless Tel. Bur. 1998) (discussing in detail the factors constituting *de facto* control); Stephen F. Sewell, *Assignments and Transfers of Control of FCC Authorizations Under Section 310(d) of the Communications Act of 1934*, 43 FED. COMM. L.J. 277, 316-17 (1991).

[47] 47 C.F.R. 1.2110(c)(2)(ii)(F); *Part 1 Fifth Report and Order*, 15 FCC Rcd at 15325-26 ¶¶ 65-66.

[48] *See Part 1 Fifth Report and Order*, 15 FCC Rcd at 15325-26 ¶ 65.

[49] *Id.*

[50] Amendment of Part 1 of the Commission's Rules - Competitive Bidding Procedures, WT Docket No. 97-82, *Third Report and Order and Second Further Notice of Proposed Rule Making*, 13 FCC Rcd 374, 478 ¶ 186 (1997) ("*Part 1 Third Report and Order*").

[51] *Part 1 Fifth Report and Order*, 15 FCC Rcd at 15293, 15323-24 ¶ 58.

[52] *Further Notice*, 21 FCC Rcd at 1754-57 ¶¶ 1, 3-5.

[53] *Id*. at 1754-55, 1759-62 ¶¶ 1, 12-18.

[54] *Id*. at 1754-55, 1762-63 ¶¶ 1, 19.

entity benefit.[55] Finally, in the *Further Notice*, we sought comment on changes to the Commission's auction application rules to facilitate the application of any rule modifications to upcoming auctions.[56]

B. Material Relationship

15. As discussed fully below, we revise our Part 1 rules to consider certain relationships as factors in determining designated entity eligibility. In so doing, we seek to improve our ability to achieve Congress's directives with regard to designated entities and to ensure that, in accordance with the intent of Congress, every recipient of our designated entity benefits is an entity that uses its licenses to directly provide facilities-based telecommunications services for the benefit of the public.[57] Specifically, except as grandfathered below, an applicant or licensee has "impermissible material relationships" when it has agreements with one or more other entities for the lease (under either spectrum manager or *de facto* transfer leasing arrangements) or resale (including under a wholesale arrangement) of, on a cumulative basis, more than 50 percent of its spectrum capacity of any individual license. Such "impermissible material relationships" render the applicant or licensee (i) ineligible for the award of designated entity benefits, and (ii) subject to unjust enrichment on a license-by-license basis. Furthermore, except as grandfathered below, an applicant or licensee has an "attributable material relationship" when it has one or more agreements with any individual entity, including entities and individuals attributable to that entity, for the lease (under either spectrum manager or *de facto* transfer leasing arrangements) or resale (including under a wholesale arrangement) of, on a cumulative basis, more than 25 percent of the spectrum capacity of any individual license that is held by the applicant or licensee. The "attributable material relationship" with that entity will be attributed to the applicant or licensee for the purposes of determining the applicant's or licensee's (i) eligibility for designated entity benefits, and (ii) liability for unjust enrichment on a license-by-license basis.

16. *Further Notice.* To define "material relationship," the *Further Notice* sought comment on the specific nature of the types of additional relationships that should trigger a restriction on the availability of designated entity benefits.[58] For instance, Council Tree initially proposed that the Commission should restrict a designated entity applicant's "material relationships," including both financial and operational agreements, in order to more carefully ensure that designated entity benefits are awarded only to bona fide eligible entities.[59] In this regard, we sought comment on what might constitute a "material financial" or "material operational" relationship. Moreover, insofar as our current rules already attribute the gross revenues of those that have relationships with designated entity applicants that confer either *de jure* and *de facto* control, we also sought comment on the type of attribution standard that we should apply to any rule modification.[60]

17. The *Further Notice* also sought comment on whether restricting certain agreements as a "material relationship" would be too harsh or unnecessarily limit a designated entity applicant's ability to gain access to capital or industry expertise.[61] Additionally, the *Further Notice* sought comment on

[55] *Id*. at 1763 ¶ 20.

[56] *Id*. at 1763-64 ¶ 21.

[57] In the legislative history of Section 309(j), Congress explains that the reason for imposing anti-trafficking restrictions and unjust enrichment payment obligations on entities that receive small business benefits is to deter "participation in the licensing process by those who have no intention of offering service to the public." H.R. REP. NO. 103-111, at 257-58 (1993) (Conference Agreement adopted House provisions, in relevant part, with amendments. H.R. CONF. REP. NO. 103-213, at 483 (1993)).

[58] *Further Notice*, 21 FCC Rcd at 1760 ¶ 13.

[59] *Id.*

[60] *Id.*

[61] *Id.* at 1761 ¶ 15.

whether there might be instances where the existence of either a "material financial agreement" or a "material operational agreement" might be appropriate and might not raise issues of undue influence.[62] In this regard, the *Further Notice* asked whether the Commission should allow designated entity applicants to obtain a bidding credit or other benefits if they had only a "material financial agreement" or only a "material operational agreement" but not both, and what factors we should consider in determining the types of relationships that might not adversely affect an applicant's designated entity eligibility.[63] Finally, we sought comment on whether a spectrum leasing arrangement should be defined as a "material relationship," and whether we should consider any other arrangements for the purposes of such a definition.[64]

18. *Comments.* Commenters are generally split regarding the level of specificity with which the Commission should define "material relationship." Several commenters urge the Commission to narrowly tailor the definition so as not to "inadvertently hinder the flow of capital" to designated entity applicants.[65] For example, Wirefree Partners argues that the Commission should "narrowly and specifically define what constitutes a material relationship" because "[s]mall businesses need the flexibility to enter into reasonable commercial agreements with other participants in the communications industry."[66] Others maintain that the reach of the Commission's policies should be very broad and that we should define "material relationship" to include both financial and operational agreements.[67] For example, Council Tree and other proponents of a broad definition maintain that the definition of material relationship should include, "without limitation, management agreements, trademark license agreements, joint marketing agreements, future interest agreements (such as puts, calls, options, and warrants), and long-term *de facto* and spectrum manager leasing arrangements."[68]

19. Rural service providers oppose the proposal to define "material relationship" in a manner that would preclude small businesses from entering into operational agreements with large wireless carriers.[69] As explained by one commenter, many small and rural wireless companies "have entered into management, marketing or other non-equity arrangements with large wireless carriers which enable them to provide quality wireless services to the rural areas they are licensed to serve."[70] Another commenter

[62] *Id.*

[63] *Id.*

[64] *Id.* at 1761 ¶ 16.

[65] *See*, *e.g.*, Comments of STX at 2; *see also* Comments of Antares at 4 ("the Commission needs to balance the public policy goal of continuing to encourage small business participation within the wireless industry against the very real need for qualified small businesses to raise capital in order to participate in wireless service auctions."); Comments of Cook Inlet at 3 ("it is particularly challenging for small companies to obtain access to financial resources necessary to support bidding and paying for even one license in a given auction, much less to construct and operate a system within the time frame mandated by the Commission's rules."); Comments of NAB at 2 ("If the Commission were to adopt unnecessarily restrictive DE rules, small businesses would be more limited in their ability to raise capital and attract investors."); Reply Comments of Ericsson at 2-3 (arguing that the Commission should not constrain access to manufacturer financing).

[66] Comments of Wirefree Partners at 7.

[67] *See, e.g.,* Comments of Council Tree at 52; Comments of Leap at 15; Comments of MMTC at 2, 9.

[68] Comments of Council Tree at 52. *See also Further Notice*, 21 FCC Rcd at 1761 ¶ 9. A number of commenters also generally appeared to support the premise of Council Tree's proposals without specifically commenting on how the Commission might define "material relationship." *See, e.g.*, Comments of MobiPCS at 1; Comments of Suncom at 1; Comments of USCC at 2-3, 5.

[69] *See, e.g.*, Comments of NTCA at 7-8; Comments of RTG at 4-5.

[70] Comments of John Staurulakis, Inc. at 3.

notes that "the Commission should not consider roaming agreements evidence of a 'material relationship' since to do so would eliminate almost every small rural carrier from enjoying DE status."[71]

20. In seeking comment on spectrum leasing, we asked "what, if any standard should be used to determine whether spectrum leasing is a material relationship for the purpose of any additional restriction on the availability of designated entity benefits that we might adopt."[72] A few commenters argued that the Commission should not reverse the guidance provided in the *Secondary Markets* proceeding.[73] As noted above, a number of others generally agreed that the Commission should adopt Council Tree's proposal for material relationships, presumably including its suggestion that leasing should be included in the types of material relationships that should trigger a Commission restriction of the award of designated entity benefits.[74]

21. *Discussion.* In defining "material relationship," we seek to balance a designated entity applicant's need for flexibility to structure its business relationships against our statutory obligation to award these small business benefits only to entities intended by statute to be eligible. In our experience in administering the designated entity program over the last several years, we have witnessed a growing number of complex agreements between designated entities and those with whom they choose to enter into financial and operational relationships. Although some of these agreements may have contributed to the wireless industry becoming a thriving sector of the nation's economy, the relationships underpinning such contracts underscore the need for stricter regulatory parameters to ensure, as Congress intended, that: (1) benefits are awarded to provide opportunities for designated entities to become robust independent facilities-based service providers with the ability to provide new and innovative services to the public; and (2) the Commission employs methods to prevent unjust enrichment.[75]

22. We agree with commenters that certain agreements have the potential to significantly influence a designated entity licensee's decisions regarding its provision of service and, therefore, also have the potential to be abused, absent the appropriate safeguards. Yet, we also recognize the concerns of many, especially rural carriers, that argue that small businesses face practical difficulties in providing service and that stress that designated entity licensees must have the ability to enter into operational contracts, such as roaming, interconnection, and switch-sharing, with other, often large, providers in order to be in a position to provide valuable telecommunications service to the public.[76]

23. In considering how to evaluate which specific relationships should trigger additional eligibility restrictions, we conclude that certain agreements, by their very nature, are generally inconsistent with an applicant's or licensee's ability to achieve or maintain designated entity eligibility because they are inconsistent with Congress's legislative intent. In this regard, where an agreement concerns the actual use of the designated entity's spectrum capacity, it is the agreement, as opposed to the party with whom it is entered into, that causes the relationship to be ripe for abuse and creates the potential for the relationship to impede a designated entity's ability to become a facilities-based provider, as intended by Congress.

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[71] Comments of RTG at 5.

[72] *Further Notice*, 21 FCC Rcd at 1761 ¶ 16.

[73] *See, e.g.,* Comments of Wirefree Partners at 8-9; Comments of CTIA at 4.

[74] *See, e.g.,* Comments of Council Tree at 52; *see generally* Comments of MobiPCS at 1; Comments of Suncom at 1; Comments of USCC at 2-3, 5.

[75] *See, e.g.*, Comments of MMTC at 6 ("some of the largest national incumbent wireless carriers have received from their DE partners exclusive access to valuable spectrum and network capacity that otherwise could have been used to offer new services and induce the national wireless incumbents to better respond to the needs of the marketplace.").

[76] *See, e.g.,* Comments of RTG at 5.

24. As we indicated in the *Secondary Markets Second Report and Order*, "Congress specifically intended that, in order to prevent unjust enrichment, the licensee receiving designated entity benefits actually provide facilities-based services as authorized by its license."[77] In that proceeding, the Commission stated that leasing by a designated entity licensee of "substantially all of the spectrum capacity of the licensee" would cause attribution that would likely lead to a loss of eligibility, and that the leasing of a "small portion" of such capacity where there was no other relationship between the parties likely would not result in a finding of attribution.[78] Although at least one commenter argues that the Commission's existing leasing rules provide adequate protection to ensure that the relationship between the parties "remains one of contract and not control,"[79] as articulated in the *Further Notice* and this decision, we are modifying our rules to include additional safeguards to our designated eligibility determinations that look beyond controlling relationships to those that have the potential to influence a designated entity in a manner contrary to that intended by Congress.

25. Building on our *Secondary Markets* policies and in consideration of the record we have before us, we modify our rules regarding eligibility for designated entity benefits for applicants or licensees that have agreements that create material relationships, as defined and explained herein. Specifically, except as grandfathered below,[80] we conclude that an applicant or licensee has "impermissible material relationships" when it has agreements with one or more other entities for the lease (under either spectrum manager or *de facto* transfer leasing arrangements) or resale (including under a wholesale arrangement) of, on a cumulative basis, more than 50 percent of its spectrum capacity of any individual license. Such "impermissible material relationships" render the applicant or licensee (i) ineligible for the award of designated entity benefits, and (ii) subject to unjust enrichment on a license-by-license basis. Furthermore, except as grandfathered below,[81] we find that an applicant or licensee has an "attributable material relationship" when it has one or more agreements with any individual entity, including entities and individuals attributable to that entity, for the lease (under either spectrum manager or *de facto* transfer leasing arrangements) or resale (including under a wholesale arrangement) of, on a cumulative basis, more than 25 percent of the spectrum capacity of any individual license that is held by the applicant or licensee.[82] The "attributable material relationship" with that entity will be attributed to the applicant or licensee for the purposes of determining the applicant's or licensee's (i) eligibility for designated entity benefits, and (ii) liability for unjust enrichment on a license-by-license basis.[83]

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[77] Promoting Efficient Use of Spectrum through Elimination of Barriers to the Development of Secondary Markets, WT Docket No. 00-230, *Second Report and Order, Order on Reconsideration, and Second Further Notice of Proposed Rulemaking*, 19 FCC Rcd 17503, 17538, 17541, 17544 ¶¶ 71, 76, 82 (2004) ("*Secondary Markets Second Report and Order*").

[78] *Id.* at 17541-42 ¶ 77.

[79] Comments of Wirefree Partners at 8.

[80] *See* discussion *infra* ¶¶ 28-30.

[81] *See id.*

[82] If a designated entity licensee disaggregates its license, determinations of impermissible and attributable material relationships will be made based upon its remaining spectrum license. For example, if a designated entity licensee disaggregates 5 MHz of a 10 MHz license, it cannot have spectrum leasing or resale arrangements for more than 2.5 MHz of spectrum, pursuant to the "impermissible material relationships" restriction, and any spectrum leasing or resale arrangements with one individual entity for more than 1.25 MHz of spectrum will result in the attribution of revenues and assets, pursuant to the "attributable material relationships" restriction.

[83] During the first five years of the license term, broadband PCS entrepreneurs that have not yet met their five-year construction requirements will be prohibited from entering into any impermissible material relationships with entities of any size. They will also be prohibited from entering into attributable material relationships if those relationships bring their attributable gross revenues or total assets above the financial caps established in section 24.709. After build-out or the first five years of the license term, broadband PCS entrepreneurs that are participating in the installment payment plan and enter into impermissible or attributable material relationships will be subject to (continued....)

26. As stated above, our experience in administering the designated entity program and our review of the record developed in response to our *Further Notice* leads us to conclude that these definitions of material relationship are necessary to ensure that the recipient of our designated entity benefits is an entity that uses its licenses to directly provide facilities-based telecommunications services for the benefit of the public; that the Commission employs methods to prevent unjust enrichment; and that our statutory-based benefits are awarded only to those that Congress intended to receive them.

27. Spectrum manager and *de facto* transfer leasing agreements and resale agreements (including wholesale arrangements) with a single entity for 25 percent and less of the designated entity licensee's total spectrum capacity on a license-by-license basis, or cumulative agreements with multiple entities for 50 percent or less of a designated entity licensee's total spectrum capacity on a license-by-license basis will continue to be reviewed under our existing designated entity eligibility rules and, pursuant to existing rules and policies, may result in unjust enrichment obligations.[84] Through the decisions we make today, we will ensure that a designated entity licensee will preserve at least half of its spectrum capacity of each of its licenses for which it has been awarded and retained designated entity benefits for the provision of service as a facilities-based provider for the benefit of the public, while still having flexibility to engage in agreements that are intended to provide it with access to valuable capital, thus better furthering the goals of the statutory designated entity program.

28. *Grandfathering and Applicability of Material Relationships.* Recognizing that there are numerous agreements in existence that might fall within our newly defined "impermissible material relationships" and "attributable material relationship," we will apply these eligibility restrictions on a prospective basis. Therefore, we will not employ our new restrictions to reconsider any designated entity benefits previously awarded to licensees prior to the release date of this *Second Report and Order* or to determine designated entity benefits in an application for a license, an authorization, or an assignment or transfer of control or a spectrum lease that was filed with the Commission before the release date of this *Second Report and Order* that is still pending approval. Accordingly, we will grandfather the existence of impermissible and attributable material relationships that were in existence before the release date of this *Second Report and Order* for the purposes of assessing unjust enrichment payments on benefits previously awarded or pending award, as discussed above. In assessing the imposition of unjust enrichment for future events, if any, we will consider unjust enrichment implications on a license-by-license basis.

29. Such relationships, are not, however, generally grandfathered for the purposes of determining an applicant's eligibility for the award of designated entity benefits in future auctions or for the purposes of determining eligibility for benefits in the context of an assignment, transfer of control, spectrum lease or reportable eligibility event after the release date of this *Second Report and Order*. Except as limited by our grandfathering provisions, the rules we adopt today will apply to all determinations of eligibility for all designated entity benefits with regard to any application filed to participate in auctions in which bidding begins after the effective date of the rules, as well as to all applications for an authorization, an assignment or transfer of control, a spectrum lease, or reports of events affecting a designated entity's ongoing eligibility filed on or after the release date of this *Second Report and Order*.[85] Grandfathering the eligibility of all prior designated entity structures that involve

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installment payment unjust enrichment pursuant to section 1.2111(c). *See* 47 C.F.R. §§ 1.2110, 1.2111, 24.709, 24.839.

[84] *See Secondary Markets Second Report and Order*, 19 FCC Rcd at 17538, 17541, 17544 ¶¶ 71, 76, 82.

[85] For example, if an applicant seeking to participate in an upcoming auction has an existing impermissible material relationship on a single license, it will be ineligible for the award of designated entity benefits in that auction, regardless of the significance of that one license in terms of the applicant's revenue or the scope of its operations. This is true even if the impermissible material relationship was entered into prior to the release of this order and thus grandfathered for purposes of unjust enrichment. Similarly, if it is an attributable material relationship at issue, then

(continued....)

impermissible and/or attributable material relationships would allow these designated entities to continue to acquire additional licenses and designated entity benefits using a structure that the Commission has determined would permit a third party to leverage improper influence over a designated entity in a manner that is inconsistent with the Congressional purposes for the designated entity program. Applying our rules in this manner is consistent with how the Commission currently determines an applicant's eligibility for designated entity benefits and how it applies its unjust enrichment obligations.

30. To address concerns of several commenters, we will, however, grandfather certain relationships that were in existence before the release date of this *Second Report and Order* in the context of eligibility for future benefits. Specifically, an applicant will not be considered to be ineligible for benefits based solely on an "attributable material relationship" or "impermissible material relationships" of certain of its affiliates (as specifically defined in section 1.2110(c)(5)(i)(C)), provided that the agreement that forms the basis of the affiliate's "attributable material relationship" or "impermissible material relationship" is otherwise in compliance with the Commission's designated entity eligibility rules, was entered into prior to the release date of this *Second Report and Order*, and is subject to a contractual prohibition that prevents the affiliate from contributing to the designated entity's total financing. The purpose of this grandfathering is to provide a means for controlling interests of existing designated entities to have an ability to seek the award of designated entity benefits in future auctions or to acquire designated entity licenses in the secondary market through new and independent affiliates, even if it is affiliated with an existing designated entity that has impermissible and/or attributable material relationships that were in existence prior to the release date of the decision.[86] The attribution rules are not affected by this grandfathering.[87] In taking this action, we seek to ensure that the additional eligibility requirements we adopt today do not unnecessarily restrict applicants seeking designated entity benefits for relationships that were previously permissible under our rules.

C. Unjust Enrichment

31. We also make changes to our unjust enrichment rules to provide additional safeguards designed to better ensure that designated entity benefits go to their intended beneficiaries.[88] As discussed below, one of our primary objectives in administering our designated entity program is to prevent unjust enrichment.[89] Accordingly, in conjunction with the eligibility restrictions we adopt above, we also modify our rules and strengthen our unjust enrichment schedule for licenses acquired with bidding credits.

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the gross revenues of the entity with which the applicant has such a relationship are counted against the applicant and may affect its eligibility.

[86] For example, Newco is an applicant seeking designated entity status in an auction in which bidding begins after the effective date of the rules. Investor is a controlling interest of Newco. Investor also is a controlling interest of Existing DE. Existing DE previously was awarded designated entity benefits and has impermissible material relationships based on leasing agreements entered into before the release date of this order with a third party, Lessee, that were in compliance with the Commission's eligibility standards prior to the effective date of the rules adopted herein. In this example, Newco would not be prohibited from acquiring designated entity benefits solely because of the existing impermissible material relationships of its affiliate, Existing DE. Newco, Investor, and Existing DE, however, would need to enter into a contractual prohibition that prevents Existing DE from contributing to the total financing of Newco.

[87] *See* 47 C.F.R. § 1.2110(b). Under the example in the preceding note, Newco would have to attribute the gross revenues of its affiliate, Existing DE, in establishing eligibility for designated entity benefits, but would not have to attribute the gross revenue of Lessee.

[88] *See id*. § 1.2111(b)-(e).

[89] *See* 47 U.S.C. § 309(j)(4)(E); *see also id*. § 309(j)(3)(C).

32. *Further Notice.* In the *Further Notice*, we sought comment on whether we should adopt revisions to our unjust enrichment rules, as proposed by Council Tree,[90] or whether we should adopt other revisions to our unjust enrichment rules.[91] The Commission also asked whether reimbursement obligations should apply if a licensee takes on new investment, or also where it enters into any new financial or operational relationship that would render the licensee ineligible for a bidding credit.[92] Pursuant to any eligibility restriction that we might adopt, we asked over what portion of the license term such unjust enrichment provisions should apply.[93]

33. Additionally, we sought comment in the *Further Notice* on Council Tree's proposal that an unjust enrichment payment should not be required in the case of "natural growth" of the revenues attributed to an incumbent carrier above the established benchmark.[94] Instead, Council Tree suggests that the reimbursement obligation should apply only where the licensee takes on new investment, or enters into any operational agreement, that would have disqualified the licensee for the bidding credit at the time of the licensee's initial application.[95]

34. *Comments.* Of the commenters discussing proposed changes in the unjust enrichment policies, some contend that the Commission should continue to apply the current unjust enrichment standard.[96] These entities argue that the current unjust enrichment rules are sufficient and provide adequate protection. Thus, they conclude that no increased regulation is needed or appropriate.[97]

35. Other commenters argue for the implementation of stricter unjust enrichment rules.[98] STX supports "stricter unjust enrichment rules so that the U.S. Treasury may be made whole in the event that a designated entity turns out to have been merely a front organized to secure bidding credits for a large incumbent wireless service provider."[99] MMTC suggests that the Commission should consider adjusting its reimbursement obligations to require 100 percent of the value of the bidding credit.[100] MMTC further suggests that "the Commission should consider expanding the unjust enrichment standard to encompass the entire license term and not just the first five years."[101]

36. *Discussion.* We agree with MMTC and STX that adoption of stricter unjust enrichment rules, applicable to all designated entities, will promote the objectives of the designated entity program. The designated entity and unjust enrichment rules were adopted to ensure the creation of new

[90] Council Tree suggested a reimbursement obligation on a licensee that acquires a license with a bidding credit and subsequently, in the first five years of its license term, makes a change in its "material relationships" that would result in its loss of eligibility for the bidding credit, or seeks to assign or transfer control of the license to an entity that would not qualify for the same level of bidding credits, pursuant to any eligibility restriction that we adopt. *Further Notice*, 21 FCC Rcd at 1763 ¶ 20; Council Tree Proposal at 15.

[91] *Further Notice*, 21 FCC Rcd at 1763 ¶ 20.

[92] *Id.*

[93] *Id.*

[94] *Id.*

[95] *Id.*; Council Tree Proposal at 16.

[96] *See, e.g.,* Comments of Aloha Partners at 5; Comments of Carroll Wireless at 8; Comments of Wirefree Partners at 14-15; Comments of Council Tree at 59.

[97] *See, e.g.,* Comments of Aloha at 5; Comments of Carroll Wireless at 8.

[98] *See, e.g.,* Comments of STX at 2; Comments of U.S. Wirefree at 4; Comments of MMTC at 15; Comments of Council Tree at 15-16.

[99] Comments of STX at 2.

[100] Comments of MMTC at 15.

[101] *Id.*

telecommunications businesses owned by small businesses that will continue to provide spectrum-based services.[102] In addition, the unjust enrichment rules provide a deterrent to speculation and participation in the licensing process by those who do not intend to offer service to the public, or who intend to use bidding credits to obtain a license at a discount and later to sell it at the full market price for a windfall profit.[103] By extending the unjust enrichment period to ten years, we increase the probability that the designated entity will develop to be a competitive facilities-based service provider.

37. We adopt the following ten-year unjust enrichment schedule for licenses acquired with bidding credits. For the first five years of the license term, if a designated entity loses its eligibility for a bidding credit for any reason,[104] including but not limited to, entering into an "impermissible material relationship" or an "attributable material relationship," seeking to assign or transfer control of a license, or entering into a *de facto* transfer lease with an entity that does not qualify for bidding credits, 100 percent of the bidding credit, plus interest, is owed. For years six and seven of the license term, 75 percent of the bidding credit, plus interest, is owed. For years eight and nine, 50 percent of the bidding credit, plus interest, is owed, and for year ten, 25 percent of the bidding credit, plus interest, is owed. If a designated entity loses its eligibility for the same level of bidding credit that it originally received for any reason,[105] including but not limited to, entering into an "impermissible material relationship" or an "attributable material relationship," seeking to assign or transfer control of a license, or entering into a *de facto* transfer lease with an entity that does not qualify for the same level of bidding credits, this unjust enrichment schedule will be applied to the difference between the original bidding credit and the bidding credit for which the designated entity, assignee, or assignor is eligible.[106]

38. In addition to revising the unjust enrichment payment schedule, we will impose a requirement that the Commission must be reimbursed for the entire bidding credit amount owed, plus interest, if a designated entity loses its eligibility for a bidding credit for any reason,[107] including but not limited to, entering into an "impermissible material relationship" or an "attributable material relationship," seeking to assign or transfer control of a license, or entering into a *de facto* transfer lease with an entity that is not eligible for bidding credits prior to the filing of the notification informing the Commission that the construction requirements applicable at the end of the license term have been met.[108] For example, if a designated entity seeks to assign a license with a bidding credit to an entity that is not

[102] *Competitive Bidding Second Report and Order*, 9 FCC Rcd at 2394 ¶ 258.

[103] *Id.* at 2385, 2394 ¶¶ 211, 259. *See also* H.R. REP. NO. 103-111, at 257-58 (1993) (Conference Agreement adopted House provisions, in relevant part, with amendments. H.R. CONF. REP. NO. 103-213, at 483 (1993)); *Secondary Markets Second Report and Order*, 19 FCC Rcd at 17538 ¶ 71.

[104] *See* discussion *infra* note 116 and accompanying text.

[105] *See* discussion *infra* note 116 and accompanying text.

[106] We also note that the provisions of section 1.2112(e) of the Commission's rules may also apply. 47 C.F.R. § 1.2112(e) (discussing the assessment of unjust enrichment in the context of the partition and/or disaggregation of licenses).

[107] *See id.*

[108] Licensees may, under section 1.946(e) of our rules, request an extension of time to meet the applicable construction requirements. 47 C.F.R. § 1.946(e). Additionally, licensees may also request a waiver of the construction requirement, and this request must meet the requirements of section 1.925 of our rules. 47 C.F.R § 1.925. We note that we will undertake careful scrutiny of requests for extension of the construction requirements filed by designated entities consistent with our rules, obligations under the Communications Act, and legal precedent, and that we will consider , as part of our review, whether the extension request is an effort to defeat the objectives of our designated entity program. If a designated entity is successful in obtaining an extension of the construction requirements beyond the initial license term, the requirement that the Commission must be reimbursed for the entire bidding credit amount, plus interest, prior to the filing of the notification informing the Commission that the applicable construction requirements will continue to apply until such notifications are filed.

eligible for bidding credits eight years after the grant of the license and prior to the filing of the construction notification, 100 percent of the bidding credit, plus interest, will be owed, rather than the 50 percent unjust enrichment payment that would have been due had the construction notification been on file with the Commission, pursuant to the revised unjust enrichment schedule, above.

39. We impose the above-mentioned reimbursement obligations on any licensee that acquires licenses with bidding credits and subsequently loses its eligibility for a bidding credit for any reason because the implementation of such a policy is consistent with the policies underlying the Commission's designated entity and unjust enrichment requirements. By expanding the unjust enrichment period and requiring full payment of the bidding credit until a license has been constructed, we are fulfilling Congress's mandate that designated entities are given the opportunity to participate in the provision of spectrum-based services, while ensuring that entities that are not eligible for designated entity benefits cannot benefit from the designated entity program by acquiring the licenses or entering into impermissible or attributable material relationships with a designated entity after it acquires a license at auction or in the secondary market.[109]

40. We agree with Council Tree's proposal that unjust enrichment payments should not be required for licenses held by the designated entity in the case of "natural" or "permissible" growth of the gross revenues of either a designated entity or an investor in a designated entity. Currently, there are no permissible growth provisions associated with bidding credits.[110] However, Commission practice has been that a designated entity will not owe unjust enrichment for its licenses if the designated entity's increased gross revenues, or the increased gross revenues of any controlling interest or affiliate, are due to nonattributable equity investments, debt financing, revenue from operations or other investments, business development, or expanded service.[111] Commission precedent states that the Commission evaluates an applicant's or licensee's eligibility for designated entity benefits and determines whether unjust enrichment is owed at the time the relevant application or notification (*e.g.,* transfer of control or assignment) is filed.[112] Under the policies adopted in this *Second Report and Order*, the Commission similarly would evaluate an applicant's or licensee's eligibility for designated entity benefit at the time it files an application regarding a reportable eligibility event, as required in the new section 1.2114 that we adopt herein. Thus, if the designated entity seeks to acquire licenses on the secondary market or in future auctions, all of the designated entity's gross revenues, along with the gross revenues of its controlling interests and affiliates, will be attributed to the designated entity.[113]

[109] *See* 47 U.S.C § 309(j)(4)(E); *see also* id. § 309(j)(3)(C).

[110] We note that, although the Commission did not adopt a permissible growth exception for bidding credit unjust enrichment, it did adopt a permissible growth exception for set-aside, or closed bidding, licenses and installment payments. *Compare* 47 C.F.R. § 1.2111(d) *with id.* §§ 1.2111(c)(2), *and id.* § 24.709(a)(2).

[111] *Cf*. 47 C.F.R. § 1.2111(c)(2) (establishing that "permissible growth" does not result in unjust enrichment in the context of installment payments); *id*. § 24.709(a)(2) (establishing that permissible growth does not result in the loss of eligibility to hold set-aside, or closed bidding, licenses).

[112] *See* Applications of TeleCorp PCS, Inc., Tritel, Inc, and Indus, Inc., WT Docket No. 00-1589, *Memorandum Opinion and Order*, 16 FCC Rcd 3716, 3737 ¶ 49 (Wireless Tele. Bur. 2000) ("*TeleCorp-Tritel Order*"); D&E Communications, Inc., *Order*, 15 FCC Rcd 61, 67 ¶ 12 (Auctions & Ind. Analysis Div., Wireless Tele. Bur. 1999) ("*D&E Communications*").

[113] *See* Amendment of Commission's Rules Regarding Installment Payment Financing for Personal Communications Services (PCS) Licenses, WT Docket No. 97-8200-1589, *Memorandum Opinion and Order*, 14 FCC Rcd 20543, 20545-46 ¶¶ 6-8 (1999); *see also TeleCorp-Tritel Order*, 16 FCC Rcd at 3734 ¶ 46; *D&E Communications*, 15 FCC Rcd at 67 ¶ 12.

41. Finally, we agree with Cook Inlet's general concern that retroactive penalties not be imposed upon pre-existing designated entities. Thus, as discussed fully above, we grandfather the applicability of these rules under certain circumstances.[114]

D. Implementation

42. In this section, we explain how we intend to utilize the tools for preventing abuse of the designated entity program that are already at our disposal in our rules, and we describe certain minor rule modifications that we adopt in order to make these tools more effective. To achieve this purpose, we will use the following combination of existing and new measures to ensure that designated entity incentives benefit solely those parties intended to receive them under both our rules and section 309(j) of the Communications Act of 1934, as amended ("Communications Act"). First, we will review the agreements to which designated entity applicants and licensees are parties. Second, we will require that applicants and licensees seek advance Commission approval for all events that might affect their ongoing eligibility for designated entity benefits. Third, we will impose periodic reporting requirements on designated entities. Fourth, we will conduct audits, including random audits, of those claiming designated entity benefits. In this section we also provide guidance as to how our rules and procedures should be followed by applicants for the upcoming Advanced Wireless Services ("AWS") auction.

43. *Review of Agreements*. In applying our controlling interest standard, Commission staff has carefully reviewed agreements between applicants claiming designated entity status and other existing wireless carriers. In these cases, staff has usually undertaken discussions with such designated entity applicants in order to obtain revisions to agreements to ensure that entities with whom they have partnered are not an attributable controlling interest or affiliate obviating the applicant's eligibility for designated entity benefits. This review is necessarily specific to each relationship, since no two sets of agreements and no two sets of factual circumstances are exactly the same.

44. In light of the steps we are taking in this *Second Report and Order* to aid our ability to ensure that only eligible entities obtain designated entity benefits, we will undertake a thorough review of the long-form application (FCC Form 601) filed by every winning bidder claiming designated entity benefits and will carefully review all relevant contracts, agreements, letters of intent, and other such documents affecting that applicant. This review remains essential to our assessment of designated entity eligibility under the controlling interest standard and will be even more critical in ensuring that the rules and policies adopted in this *Second Report and Order* are fully effectuated. Thus, we will require that all designated entity applicants that are winning bidders at an auction file all relevant contracts, agreements, letters of intent, and other such documents affecting that applicant as part of the long-form application (FCC Form 601). In order to implement this rule, we delegate to the Bureau the authority to determine the method for designated entities to submit the appropriate and relevant documents. We note, however, that no licenses will be granted until all relevant contracts, agreements, letters of intent, and other such documents affecting that applicant are finalized.

45. Further, we will also thoroughly review all relevant contracts, agreements, letters of intent, and other such documents affecting an applicant, which claims designated entity eligibility, seeking to acquire licenses with designated entity benefits in the secondary market (*e.g.,* transfers of control, assignments, spectrum manager leases). Commission staff has requested such documents from entities acquiring designated entity licenses in the secondary market, especially when the applicant is a newly-created entity that has not been passed on as a designated entity in the past or where it appears that the corporate structure of a designated entity has changed. Thus, we will, as we have in the past, request designated entity applicants to forward copies of their agreements to Commission staff for review.

[114] *See* discussion *supra* ¶¶ 28-30 (discussing the grandfathering of impermissible and attributable material relationships that were in existence before the release date of this *Second Report and Order* for the purposes of assessing unjust enrichment penalties on benefits previously awarded).

46. *Event-Based and Annual Reporting Requirements*. In light of the changes that we are making to the designated entity rules, the Commission will require additional information from applicants and licensees in order to ensure compliance with the policies and rules adopted herein. We also hereby adopt rules as shown in Appendix B, authorizing modifications to be made, as necessary, to and the creation, if necessary, of FCC forms to implement the rule changes adopted herein. Although many of these rule changes are minor, we highlight the following changes to our rules. Specifically, we adopt a new rule, section 1.2114, to require that designated entities seek approval[115] for any event in which they are involved that might affect their ongoing eligibility,[116] even if the event would not have triggered a reporting requirement under our rules.[117] Such events – known as "reportable eligibility events" – will also include those that result in an "impermissible material relationship" or an "attributable material relationship." We note that applications seeking approval of these "reportable eligibility events" will be considered substantial (*i.e.,* not *pro forma*) pursuant to the Commission's rules or precedent and will not be approved until any applicable unjust enrichment is paid.

47. Additionally, we will revise section 1.2110 of the Commission's rule to require designated entity licensees to file an annual report with the Commission, which will, at a minimum, include a list and summaries of all agreements and arrangements (including proposed agreements and arrangements) that relate to eligibility for designated entity benefits. In addition to a summary of each agreement or arrangement, this list must include the parties (including affiliates, controlling interests, and affiliates of controlling interests) to each agreement or arrangement, as well as the dates on which the parties entered into each agreement or arrangement. Annual reports will be filed no later than, and up to five business days before, the anniversary of the designated entity's license grant.[118]

48. We consider adoption of these reporting requirements to be a foreseeable component of the designated entity eligibility rules we adopt today, and we believe them to be necessary to the successful implementation of these rules. We also consider these requirements to be an extension of the existing responsibility of designated entities to retain and make available, on an ongoing basis, all agreements related to their eligibility.[119] Furthermore, we delegate to the Bureau the authority to implement the necessary modifications to FCC forms and the Universal Licensing System (ULS) to implement these rule changes and to determine the content of, and filing procedures for, the new annual filing requirement.

49. *Audits*. Pursuant to our existing rules, the Commission has broad power to conduct audits at any time and for any reason, including at random, of applicants and licensees claiming designated entity benefits.[120] In its comments, MMTC urges the Commission to employ its existing audit power and

[115] Obtaining prior approval for events that could possible effect an entity's designated entity eligibility is consistent with our practices for reviewing applications for the assignment or transfer of control of designated entity licenses. *See* 47 C.F.R. § 1.948(c)(1)(i).

[116] Such events include changes in the ownership structure of the designated entity and agreements (*e.g.,* management, credit, trademark, marketing, and facilities agreements) entered into between designated entity licensees and third parties that the Commission has not previously reviewed. New section 1.2114(c) provides that such filings will be treated as if they are transfer of control applications under section 1.1102 for purposes of determining the appropriate application fees.

[117] 47 C.F.R. § 1.948(j).

[118] The record supports such an approach. *See, e.g.* Comments of Cook Inlet at 21 (suggesting that the Commission require each designated entity to submit an annual report detailing the actions it took during the past period with respect to the licenses it holds as well as any actions taken by its limited financial partners. It believes that the Commission would have some empirical evidence of the degree of day-to-day control actually exercised by the parties who purport to be in *de facto* control of these designated entity licensees).

[119] *See* 47 C.F.R. § 1.2110(j).

[120] *See id.* § 1.2110(j), (n).

regularly conduct random audits to "uncover manipulation of the [designated entity] program irrespective of the type of business in which a [designated entity] applicant's partner is engaged."[121] MMTC recommends that these audits "incorporate site visits to offices and physical plants, interviews with staff and meaningful inquiries into the management of the licenses," explaining that these efforts would be "more likely to yield discoveries of improper activity than cursory paper-base[d] audits which would allow the audited entity to craft creative responses to audit requests."[122] Cook Inlet, in suggesting the imposition of periodic reporting requirements, noted above, explains that such requirements, along with "the possibility of a further audit[,] might dissuade some abuse of the Commission's rules. . . ."[123]

50. We agree that our audit authority is an effective method by which to ascertain the initial and ongoing eligibility of the claimants of designated entity benefits. Applicants and licensees should therefore understand that the Commission can and will audit their continued designated entity eligibility as circumstances may necessitate or at will. Moreover, based on the significance of the upcoming AWS auction, we commit to audit the eligibility of every designated entity that wins a license in that auction at least once during the initial license term. In order to effectively conduct these audits, we delegate to the Bureau the authority to implement and create procedures to perform such audits.

51. *Pending Auction Provisions*. As noted in the *Further Notice*, we intend any changes adopted in this proceeding to apply to AWS licenses currently scheduled to be offered in an auction beginning June 29, 2006.[124] We noted that in light of the current auction schedule, any changes that we adopt in this proceeding may become effective after the deadline for filing applications to participate in that auction. We sought comment on our proposal to require applicants to amend their applications on or after the effective date of the rule changes with a statement declaring, under penalty of perjury, that the applicant is qualified as a designated entity pursuant to section 1.2110 of the Commission's rules effective as of the date of the statement.[125] We also noted that in the event applicants fail to file such a statement pursuant to procedures announced by public notice, they will be ineligible to qualify as a designated entity.[126]

52. The vast majority of commenters did not address this issue.[127] Under Commission rules, applicants asserting designated entity eligibility in a Commission auction are required to declare, under penalty of perjury, that they are qualified as a designated entity under section 1.2110 of the Commission's

[121] Comments of MMTC at 13-14.

[122] *Id.* at 14.

[123] Comments of Cook Inlet at 21.

[124] Auction of Advanced Wireless Services Licenses Scheduled for June 29, 2006, Comment Sought on Reserve Prices or Minimum Opening Bids and Other Procedures, AU Docket No. 06-30, *Public Notice*, 21 FCC Rcd 794 (2006).

[125] *Cf.* 47 C.F.R. 1.2105(a)(2)(iv) (parallel statement currently required as of the date of filing the short-form application). Pursuant to its delegated authority to conduct auctions, the Wireless Telecommunications Bureau will establish any detailed procedures necessary for making required amendments and announce such procedures by public notice. *See id.* §§ 0.131, 0.331.

[126] As noted in the *Further Notice*, while prior certifications may be a prerequisite to eligibility, applicants still must demonstrate compliance with all applicable Commission rules, including eligibility for any bidding credits, at the time the Commission is ready to grant a license, regardless of previously applicable rules. *See* Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, *Report and Order*, 21 FCC Rcd 891, 909 n.84 (2006); *see also Celtronix Telemetry, Inc. v. FCC*, 272 F.3d 585, 587 (D.C. Cir. 2001), *cert. denied*, 536 U.S. 923 (2002) (affirming Commission application of installment payment rules that were revised after initial grant of license).

[127] While CTIA expresses some concern regarding the amendment of short form applications, the public interest benefits associated with requiring entities to amend their applications and certify that they are qualified as a designated entity pursuant to our modified rules, outweigh any concerns raised in the record.

rules.[128] After reviewing the record and considering the public interest benefits associated with our proposal, we will require entities applying as designated entities to amend their applications for the AWS auction on or after the effective date of the rule changes with a statement declaring, under penalty of perjury, that the applicant is qualified as a designated entity pursuant to section 1.2110 of the Commission's rules effective as of the date of the statement.

IV. SECOND FURTHER NOTICE OF PROPOSED RULE MAKING

53. As noted above, in reviewing the record in this proceeding, including the requests of various parties to conduct a further inquiry,[129] we issue this *Second Further Notice* to consider whether we should modify further our general competitive bidding rules[130] governing benefits reserved for designated entities.[131]

54. Specifically, we seek further guidance on whether the Commission should implement additional safeguards beyond those we adopt today to ensure that our designated entity benefits are awarded to the entities and for the purposes intended by Congress. Additionally, we are seeking comment to obtain additional economic evidence regarding how and under what circumstances an entity's size might affect its relationships and agreements with designated entity applicants and licensees. As discussed fully below, we therefore seek further comment on whether we should adopt additional rule changes that would restrict the award of designated entity benefits under certain circumstances and in connection with relationships with certain entities.

A. Defining the Class

55. *Further Notice.* In the *Further Notice*, we sought comment on Council Tree's suggestion for defining the elements of an eligibility restriction to apply to those that Council Tree referred to as "large in region incumbent wireless providers" that had "average gross wireless revenues"[132] for the preceding three years exceeding $5 billion. We sought comment on this proposed benchmark and whether it was a useful element for consideration if we adopt our tentative conclusion to modify our Part 1 rules to include additional restrictions on the availability of designated entity benefits. We asked whether $5 billion was an appropriate level at which to set the benchmark to define those with whom a designated entity applicant's material relationships would trigger a restriction on the award of benefits. In contemplating this proposal, we sought comment on whether we should consider "gross wireless revenues" as suggested by Council Tree or instead whether we should generally consider "gross revenues" as defined in section 1.2110(n) of the Commission's rules.[133]

56. The *Further Notice* also sought comment on whether we should instead apply the restriction to the award of designated entity benefits where an applicant had a material relationship with "entities with significant interests in communications services" in order to extend the scope of such a restriction to a broader category of businesses such as voice or data providers, content providers, equipment manufacturers, other media interests, and/or facilities or non-facilities based communications services providers. We sought comment on whether all of these entities should be included as part of our definition of "entities with significant interests in communications services" or whether we should consider excluding some of these entities from our proposed definition. We also sought comment on whether we should consider including other entities as part of our proposed definition.

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[128] *See* 47 C.F.R. § 1.2105(a)(2)(iv).

[129] *See, e.g.*, Comments of NHMC at 17-18; Reply Comments of Consumers Union at 1-2.

[130] *See* 47 C.F.R. § 1.2101 *et seq.*

[131] *See supra* note 8 (discussing the Commission's designated entity benefits).

[132] Council Tree's proposal does not include a definition of "average gross wireless revenues."

[133] 47 C.F.R. § 1.2110(n).

57. *Comments.* Commenters were generally divided regarding how the Commission should define this particular element of its rule modification. Those commenters who supported the proposal in the *Further Notice* to define the class to include "large incumbent wireless service providers" were divided on the thresholds that we should consider. Some commenters advocated defining the term "large" in accordance with financial thresholds,[134] while others supported a threshold based on subscription levels.[135] Some commenters who supported using financial thresholds advocated a restriction based upon average gross revenues for the preceding three years exceeding $5 billion.[136] One commenter believed that the threshold should be $1 billion.[137] Commenters were split on whether we should consider "gross wireless revenues" or generally consider "gross revenues" as defined in section 1.2110(n) of the Commission's rules.[138] Commenters that opposed the use of a $5 billion revenue threshold believed that this threshold was arbitrary, with no factual or public interest basis.[139]

58. Several commenters argued that if the Commission adopted any additional eligibility restrictions, it should extend the scope of the prohibition beyond "large incumbent wireless service providers." For example, T-Mobile argued that no justification exists for excluding large, multinational conglomerates from the prohibition. It suggested that if the Commission's goal is to ensure small business bidders are actually small businesses, excluding large corporations defeats the proposed designated entity rule reform.[140] Similarly, Verizon Wireless asserted that prohibiting partnerships with large, incumbent wireless service providers, but not other wireless carriers or companies, will not impact the legitimacy of a designated entity or fulfill the Commission's goals. If the Commission opts to impose restrictions on designated entities, Verizon Wireless stated the proposed changes should affect all designated entities and all of the designated entity's partners.[141] In addition, USCC suggested that the same adverse effects that can occur in designated entity relationships with national incumbent wireless service providers can also occur with the nation's largest voice and data providers, content providers, media interests, equipment manufacturers and facilities based and non-facilities based communication services providers.[142]

59. *Second Further Notice*. We acknowledge that voice, data, and video services are converging and are being offered as bundled service packages. These bundled service offerings may include wireline, wireless, cable and or DBS services along with the required equipment such as handsets and receivers. In light of the continuing dynamic technological developments and convergence occurring in the communications marketplace, we seek comment on the appropriate class of entity, if any, that should trigger to trigger any additional restriction we may adopt regarding relationships with designated

[134] *See, e.g.,* Comments of Council Tree at 33; Comments of Leap at 15; Comments of MetroPCS at 9.

[135] *See, e.g.,* Comments of MMTC at 9.

[136] *See, e.g.,* Comments of Council Tree at 33; Comments of Leap at 15; Comments of MetroPCS at 9. These commenters believe that this threshold is an objective measure to address carriers with operations that can be characterized as national in scope and scale, and that designated entities who partner with companies meeting this threshold are the least likely to provide services that compete with the service provided by these large companies.

[137] *See, e.g.,* Comments of Centennial at 6.

[138] *See, e.g.,* Comments of Council Tree at 33-34; Comments of USCC at 10 (advocating the use of gross wireless revenues).

[139] *See, e.g.,* Comments of CTIA at 3, 5, 11; Comments of T-Mobile at 9; Comments of Verizon Wireless at 19-20 ("If the Commission wished to set a threshold for strategic investment in designated entities, it should set the standard at the level it adopted for the Entrepreneurs Block, which is $125 million in revenues measured over two preceding years.").

[140] Comments of T-Mobile at 8.

[141] Comments of Verizon Wireless at 4-6.

[142] Comments of USCC at 11-13.

entities. For instance, would the Commission be better positioned to achieve its statutory mandates if it defined such an entity to include one that is subject to the Commission's jurisdiction under Titles I, II, III, or VI of the Communications Act, including any of the entity's controlling interests or affiliates as those terms are defined in section 1.2110 of the Commission's rules (herein after "attributable communications entity"). Insofar as this definition captures a varied class of potential partners, including not only entities that have CMRS spectrum, but also wireline, broadcast, cable, satellite, and VoIP providers, would restricting certain relationships between designated entities and such a class better safeguard the award of designated entity benefits?

60. We seek comment on whether adopting a definition of a class of entities with whom a designated entity's agreements might trigger additional restrictions for designated entity benefits will better ensure that the Commission can continue to award such benefits to entities that Congress intended. Does one class of entities have a greater incentive and/or ability than another to attempt to acquire licenses at below market prices by using agreements with a designated entity?

61. We also seek comment on the financial threshold that we should consider in defining the appropriate class of entity that would trigger an eligibility restriction. As noted above, commenters were divided on the appropriate financial threshold. We seek further comment on the proposed financial benchmarks raised by the commenters. Should we consider a financial threshold of $5 billion in annual gross revenues as advocated by various parties or lower thresholds such as $1 billion or $125 million as suggested by other commenters? Is the entity's size in terms of either its gross revenues or some other benchmark relevant to its incentive and/or ability to enter into agreements with a designated entity in a manner designed to gain access to benefits it is otherwise not eligible to obtain? We also seek comment on whether an entity's size is relevant to its incentive and/or ability to influence the designated entity with respect to the type and scope of the service it might provide as well as relevant economic analysis to support such arguments.

62. Similarly, we seek comment on whether we should define a class of entities based on its particular spectrum interests, for instance those that have licenses for "commercial mobile radio services spectrum" ("CMRS spectrum"). If we were to define a class in this manner, should we define CMRS spectrum to include "any spectrum for which the service specific rules permit the provision of commercial mobile radio services" as that term is defined in section 20.9 of the Commission's rules?[143] We also seek comment on whether an entity's existing spectrum interests are relevant to the likelihood of it seeking to influence the designated entity with respect to the type and scope of the service it might provide as well as relevant economic analysis to support such arguments. If we determine to base any additional safeguards upon an entity's particular spectrum interests, should we consider including spectrum other than CMRS spectrum for the purposes of such restrictions? If so, what spectrum and why is it more or less relevant than other types of spectrum?

B. In-Region Limitation for Class of Entities

63. *Further Notice*. In the *Further Notice*, we sought comment on whether geographic overlap should be an element in establishing any additional restriction on the availability of designated entity benefits for entities that have a "material relationship"[144] with a large wireless service provider. We also sought comment on whether we should apply a different, or any, geographic standard if we extend the restriction on designated entity benefits to applicants that have material relationships with "entities with significant interests in communications services." In addition, we asked whether we should apply the standard set forth in the former spectrum aggregation rule to define the geographic overlap,[145] as

[143] 47 C.F.R. § 20.9.

[144] Letter from Messrs. Steve C. Hillard and George T. Laub, Council Tree Communications, Inc. to Marlene H. Dortch, Secretary, Federal Communications Commission, WT Docket Nos. 02-353, 04-356, RM-10956 (June 13, 2005) (Council Tree *ex parte*).

[145] 47 C.F.R. ¶ 20.6(c) (sunset January 1, 2003).

proposed by Council Tree, or if we should adopt a different definition of geographic overlap. Further, we sought comment on how the Commission should implement such a restriction if we determined that a significant geographic overlap did exist. We asked whether an incumbent should be allowed to divest its interest in the subject service area to allow a designated entity applicant to maintain eligibility for a bidding credit, and if so, within what time period should we require the divestiture. We also sought comment on whether the application of the standard set forth in Section 20.6(c) of the Commission's rules or any other geographic overlap restriction would place an undue administrative burden on the Commission, making it difficult to monitor an applicant's compliance with any adopted geographic overlap restriction.[146]

64. *Comments*. In response to the *Further Notice*, the Commission received comments both in support of and against an in-region element to any further designated entity restrictions. Some commenters agree that geographic overlap should be an element in establishing any additional restriction on the availability of designated entity benefits.[147] Generally, the proponents of a geographic overlap element state that any additional restriction should address the dominance of service providers in their existing service regions.[148] They argue that Commission regulations designed to promote competition and diversity have generally included geographic components.[149] They further argue that such an in-region component is necessary because designated entities will not compete against a large wireless provider investor in-region.[150] A few commenters also argue that the in-region component should be extended to include wireline carriers, because the presence of the wireline provider in region translates into the loss of a direct competitor.[151]

65. Many of these commenters suggest using the significant overlap, attributable interest, and divestiture standards from the sunset CMRS spectrum aggregation limit pursuant to section 20.6(c)(2) of the Commission's rules.[152] They assert that a new rule could provide that "significant overlap of an AWS-1 licensed service area and CGSA(s) . . . or SMR or PCS service area(s) occurs when at least 10 percent of the population of the AWS-1 licensed service area for the counties contained therein, as determined by the latest decennial census figures as compiled by the Bureau of Census, is within the CGSA(s) and /or SMR and/or PCS and /or AWS-1 service area(s)."[153] Other commenters argue that the Commission cannot "simply readopt [an] old rule" without reviewing the appropriateness of the overlap definition in light of current market conditions.[154] Similarly, USCC suggests that using the section 20.6 standard is no longer an adequate metric for the emerging generation of mobile services that include voice, data, video and other broadband capabilities.[155] USCC proposes that the Commission, in defining

[146] *Further Notice*, 21 FCC Rcd at 1762 ¶ 18.

[147] *See, e.g.,* Comments of Council Tree at 43; Comments of Leap at 6, 15-16; Comments of MMTC at 9-10; Comments of USCC at 9; Comments of Wirefree Partners at 11; Comments of Centennial at 8-9; Comments of STX at 3; Comments of Antares at 5-6.

[148] *See, e.g.,* Comments of Council Tree at 42.

[149] *See, e.g., id*.; Comments of NAB at 3.

[150] *See, e.g.,* Comments of Council Tree at 42.

[151] *See, e.g.,* Reply Comments of Blooston at 5; Comments of NHMC at 12.

[152] *See, e.g.,* Comments of Council Tree at 43; Comments of MMTC at 9-10; Comments of USCC at 9; Comments of Wirefree Partners at 11; Comments of Centennial at 8-9; Comments of STX at 3.

[153] Comments of Council Tree at 44.

[154] Comments of Verizon Wireless at 17 (noting that this standard was created in a different spectrum environment, one in which there were two cellular providers and 50 MHz available in each market.). *See also* Comments of USCC at 9.

[155] Comments of USCC at 9.

in-region, adopt a threshold based on the total MHz-Pops of attributable cellular, PCS, SMR and AWS spectrum held by an entity that has in-region CMRS spectrum in the relevant geographic market. Consequently, USCC asserts that an entity that has in-region CMRS spectrum would be deemed to have a "significant geographic overlap," if it has more than 30 MHz of combined cellular, PCS, SMR, and AWS holdings in the 10 percent overlap area, as defined by section 20.6(c) of the Commission's rules.[156]

66. Other commenters state that significant overlap should not be a factor in determining eligibility for small business benefits.[157] For example, DOJ argues that the restriction should apply equally to any affiliate of a designated entity whether "the affiliate is a large in-region wireless provider, an out-of-region wireless provider (which includes carriers seeking to expand their coverage footprint), or entities with significant interests in other communications services."[158] CTIA alleges that an in-region component is discriminatory as it favors wireless, wireline and non-communications competitors over "in market" providers without any evidence of market concentration.[159] CTIA further argues that the in-region element is unnecessary, because most large service providers would be barred from entering into relationships with designated entities due to the 10 percent population overlap threshold proposed in the *Further Notice*.[160]

67. Many of the opponents of an in-region component argue that consideration of significant geographic overlap is not necessary to achieving the Commission's goals.[161] For instance, Verizon Wireless states that "restricting a designated entity's ability to partner with an incumbent, but not with other wireless carriers or companies will have no impact on whether that designated entity is legitimate or whether the Commission's objectives for small businesses are fulfilled."[162] MetroPCS alleges that national carriers should be excluded by the restriction even if a designated entity, associated with a large carrier, acquired spectrum in a market where it currently holds spectrum, because the designated entity is less likely to introduce innovative products and services.[163] Another commenter argues that we should not allow large carriers to neutralize what may be the critical advantage to a new, independent entrant and that a large carrier that desires to establish an in-region presence can participate in the auction directly.[164] One commenter also states that an in-region component would only create a source of abuse or confusion involving the proper calculation of overlap areas.[165]

68. *Second Further Notice.* In this *Second Further Notice*, we seek further comment on whether we should adopt an in-region component to defining relationships with any particular class or type of entity that trigger additional eligibility restrictions. We request that commenters address whether adopting an in-region component to the restriction of relationships furthers the objectives of the designated entity program. We seek comment as to whether the in-region component will ensure that licensees receiving small business benefits will be independent, facilities-based service providers. We ask commenters to discuss how the in-region element will ensure that designated entities are free from

[156] *Id*.

[157] *See, e.g.,* Comments of MetroPCS at 10; Comments of NHMC at 3, 4; Comments of CTIA at 11-14 ; Comments of U.S. Wirefree at 3; Reply Comments of Consumers Union at 2-3; Comments of Verizon Wireless at 6; U.S. Department of Justice *ex parte* at 6.

[158] U.S. Department of Justice *ex parte* at 6.

[159] Comments of CTIA at 1-2.

[160] *Id.* at 13-14.

[161] *See, e.g.,* Comments of U.S. Wirefree at 3; Comments of MetroPCS at 10; Comments of Verizon Wireless at 6.

[162] Comments of Verizon Wireless at 6.

[163] Comments of MetroPCS at 10.

[164] Comments of NMHC at 8.

[165] Comments of U.S. Wirefree at 3-4.

undue influence from either larger or self interested entities with whom they enter into relationships. We request that commenters discuss whether the in-region component should apply to all definitions of additional eligibility restrictions and if not, commenters should explain why the in-region component should be defined or applied differently. We also seek comment on whether all entities with in-region spectrum interests have the same ability and incentive to leverage an inappropriate level of influence over a designated entity with which it has financial and/or operational arrangements. We seek comment on how the in-region component protects this program from being subject to potential abuse from those restricted entities that might seek to craft relationships with designated entity applicants in a manner intended to serve their self interests.[166]

69. Assuming we do adopt an in-region component to any additional eligibility restrictions, we seek comment as to whether we should find that a "geographic overlap" that triggers the in-region restriction occurs when there is *any* overlap between the licensed service areas of the entity that has in-region spectrum, with whom the designated entity applicant has a "material relationship," or any affiliate of the entity that has in-region spectrum as defined in section 1.2110 of the Commission's rules,[167] and the licensed service area to be acquired by the designated entity applicant. Should this restriction apply only to particular types of spectrum – for example, only CMRS spectrum? We also seek further discussion of how the "significant overlap" standard set forth in the former spectrum aggregation limit would apply if it were adopted.[168] Generally, under that provision, "significant overlap" occurred when there was an overlap of at least ten percent of the population within the affected service areas.[169] That significant overlap standard, however, at times was problematic to apply in particular cases, for instance, because of difficulty in determining the relevant service area.[170] The Commission has stated that as a general matter it is preferable to have rules for wireless spectrum that facilitate ease of compliance and administrative efficiency.[171] Commenters addressing this issue should discuss whether reliance on the "significant overlap" test from the spectrum aggregation rule, or some variant of this test, could be crafted to facilitate ease of compliance and administrative efficiency. We also ask if the adoption of that standard would be appropriate in today's marketplace.[172] The intent of the spectrum aggregation limit at its inception was to create a competitive marketplace for CMRS as PCS licenses were being introduced. We now have a competitive wireless marketplace and any revisions to the designated entity rules that we seek

[166] *Secondary Markets Second Report and Order*, 19 FCC Rcd at 17538 ¶¶ 71, 72 (citing H.R. Rep. No. 103-111, at 257-58 (1993) (Conference Agreement adopted House provisions, in relevant part, with amendments. H.R. Conf. Rep. No. 103-213, at 483 (1993).)).

[167] 47 C.F.R. § 1.2110(c)(5).

[168] *Id*. § 20.6(c).

[169] *Further Notice*, 21 FCC Rcd at 1762 ¶ 18 (citing 47 C.F.R § 20.6(c)).

[170] For example, the rule used the term "PCS licensed service area" for determining the presence of "significant overlap" with other PCS, cellular or SMR service areas. 47 C.F.R. § 20.6(c)(1). PCS spectrum, however, is licensed on both an MTA and BTA basis, and licensees have further partitioned these areas into smaller geographic areas, which may be defined by pre-existing geographic boundaries (*e.g.*, county lines) or may be defined by the parties to a partitioning application. Licensees and applicants often faced confusion in assessing significant overlap as to which "service area" – which of the originally defined geographic areas (if there was more than one) and/or the partitioned area – should be used as the denominator.

[171] *See* 1998 Biennial Regulatory Review Spectrum Aggregation Limits for Wireless Telecommunications Carriers, WT Docket No. 98-205, *Report and Order*, 15 FCC Rcd 9219, 9226 ¶ 11 (1999).

[172] That standard was developed in conjunction with the implementation of a 45 MHz spectrum cap, as a simplified version of the Herfindahl-Hirschman Index using spectrum capacity as the measurement of market share, to limit the amount of license spectrum capacity that any one entity could have. *See* Amendment of Parts 20 and 24 of the Commission's Rules – Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap, WT Docket No. 96-59, *Report and Order*, 11 FCC Rcd 7824, 7869-70 ¶ 96 (1996).

to implement are for the purpose of ensuring that designated entity benefits do not flow to ineligible entities.

70. Further, we seek comment as to whether the adoption of an in-region component to any of any additional eligibility restrictions will be burdensome to implement. Specifically, we recognize that defining the geographic areas of the variety of services provided by certain entities will be complicated. Thus, we ask that commenters discuss how the in-region definition would take into account the different, and sometimes difficult to determine, geographic area of services provided by varying entities and how these areas of service should be compared to the Commission's wireless licensing areas.

71. *Divestiture*. Most entities responding to the *Further Notice* declined to discuss whether a restricted entity should be allowed to divest its interest in the subject service area to allow a designated entity applicant to maintain eligibility for designated entity benefits. Thus, we seek comment as to whether any class of entities on which any additional eligibility restriction is based should be allowed to divest its interest in the subject service area to allow a designated entity applicant to maintain eligibility for benefits. We also seek comment as to whether the Commission should adopt divestiture provisions similar to those found in the eliminated spectrum aggregation limit rules.[173] Moreover, we seek comment on the opinions of some commenters responding to the *Further Notice* that divestiture should not be permitted as it will "significantly complicate the auction process," lead to post-auction petitions and challenges that could delay the deployment of spectrum,[174] and allow restricted entities "to game the system by divesting *after* the auction when it can compare the merits of what it has won with what it holds already."[175]

72. If we were to allow divestitures, we seek comment as to how such divestitures should be implemented. We seek comment as to how long restricted entities that choose divestiture will be given to divest (*e.g.,* 60 days, 90 days, or 180 days), what commences the divestiture period (*e.g.,* the close of the auction, the public notice announcing the winning bidders, or the filing of the FCC Form 601), and would the restricted entity be allowed to market the spectrum or should such marketing be done by a trustee. Further, we seek comment as to whether the award of designated entity licenses should be withheld until the restricted entity files the applications to divest or until the transaction to sell the divestiture spectrum has been consummated.[176] We also seek comment as to whether the Commission should receive reports detailing the progress made in identifying a buyer for the divestiture spectrum and how often such reports should be filed.

73. Finally, we ask commenters to discuss what should occur if the restricted entity that has in-region spectrum fails to divest. We seek comment as to whether the designated entity must purchase the license without the benefit of the bidding credit and be subject to the Commission's default rules. We also seek comment as to whether the requirement for a designated entity to purchase the license without the bidding credit maintains auction integrity and ensures that entities with in-region CMRS spectrum are not able to game the auction process. What if the designated entity benefit at issue concerns eligibility for auction participation such as in the context of auctions for set-aside spectrum licenses?

C. Material Relationships

74. *Further Notice*. In examining whether certain relationships should be relevant to an applicant or licensee's ability to be eligible for designated entity benefits, the *Further Notice* sought

[173] *See* Comments of Council Tree at 45 (citing 47 C.F.R. § 20.6(e)).

[174] *See* Comments of MetroPCS at 11.

[175] Comments of Centennial at 8-9 (emphasis in original).

[176] We would consider adopting such a divestiture procedure because we want to ensure that there is an identified buyer for the divestiture spectrum prior to the grant of the designated entity license.

comment on the specific nature of the types of relationships that should trigger any restriction.[177] Council Tree's initial proposal argued that the Commission should restrict a designated entity applicant's "material relationships," including both financial and operational agreements, in order to more carefully ensure that designated entity benefits are awarded only to bona fide eligible entities.[178] In this regard, we sought comment on what might constitute a "material financial" or "material operational" relationship; whether restricting certain agreements as a "material relationship" would be too harsh or unnecessarily limit a designated entity applicant's ability to gain access to capital or industry expertise[179]; and whether there might be instances where the existence of either a "material financial agreement" or a "material operational agreement" might be appropriate and might not raise issues of undue influence.[180] We also sought comment on the type of attribution standard that we should apply to any rule modification.[181]

75. *Comments*. In the record developed in connection with the *Further Notice*, many commenters supported the general premise of Council Tree's proposal to define "material relationships" to include even those agreements that would preserve a designated entity applicant's *de jure* and *de facto* control under our existing rules.[182] Several commenters argued that the Commission's controlling interest standard does not, without more, sufficiently safeguard the award of designated entity benefits to their intended beneficiaries because it does not adequately insulate the designated entity from undue influence.[183]

76. Commenters opposing rule modifications to consider such relationships; however, argued that there is insufficient evidence to support such rule changes, and maintain that there is no record of abuse of the Commission's designated entity eligibility requirements.[184] Moreover, opposing commenters

[177] *Further Notice*, 21 FCC Rcd at 1760 ¶ 13.

[178] *Id.*

[179] *Id.*

[180] *Id.* at 1761 ¶ 15.

[181] *Id.*

[182] Comments of Council Tree at 52; *see also generally*, Comments of Anatres; Comments of Carroll Wireless; Comments of Doyon Communications, Bristol Bay Native Corp., Bethel Native Corp.; Comments of John Staurulakis, Inc.; Comments of Leap; Comments of MMTC; Comments of STX; Comments of Suncom; Comments of USCC; Comments of U.S. Wirefree.

[183] *See, e.g.*, Comments of Council Tree at 55-56 ("the Commission's existing "controlling interest" standard and affiliation rules do not prevent the type of influence that should be addressed here."); Comments of MobiPCS at 1 ("allowing the nation's largest national wireless carriers to serve in those roles only serves to increase their already overwhelming influence."); Comments of WBSPA at 4-5("WBPSA strongly supports the proposals put forth by CT to eliminate and prohibit any ability for any communications services provider whose services are regulated by the FCC or any state regulatory body to enter into any financial relationship with an otherwise eligible DE in which it has the ability to either directly or indirectly control or influence the management, operations or ownership of that entity. . . ."). *But see* Reply Comments of WBSPA at 2 (WBSPA refined and clarified its position to apply to "any communications service providers whose telecommunications activities are subject to state or federal telecommunications regulations and whose revenues exceed $1 billion in the last calendar year. . . .").

[184] *See, e.g.,* Comments of CTIA at 2 ("there is no evidence cited in the Notice that those policies have been abused, that they have not been effective, or that their reformation would achieve any stated goal."); Comments of T-Mobile at 6 ("The Commission cites no evidence to demonstrate – indeed, it makes no allegations – that such wireless carriers have attempted to circumvent the letter or spirit of the Commission's DE rules or have otherwise been responsible for 'undermining' the program."); Comments of Verizon Wireless at 4 (the FNPRM "fails to cite evidence that any harm has resulted from strategic relationships between small businesses and large wireless carriers."); Comments of Cook Inlet at i, 5 ("Cook Inlet is concerned by the absence of a factual record that justifies a rule change of the magnitude proposed in the *Further Notice*.").

contended that if the Commission is compelled to amend its rules, adoption of its tentative conclusion will not be sufficient to accomplish its intended purpose.[185]

77. Both sides offered general comments regarding whether the Commission should take non-controlling relationships into consideration as part of its determination of an applicant's or licensee's eligibility for designated entity purposes, but few offered specifics on how the Commission should precisely define material relationships. As discussed above, we have adopted two definitions of material relationships. The first are "impermissible material relationships" that, when entered into by an applicant or licensee, will render it wholly ineligible for designated entity benefits. The second are "attributable material relationships." These relationships become attributable for the purposes of calculating the applicant or licensee's eligibility for benefits in accordance with section 1.2110 of the Commission's rules.

78. *Discussion.* We seek comment on whether there is a need, in addition to the rules we adopt today, to further modify our Part 1 designated entity eligibility rules to include other types of agreements in our definitions of "impermissible material relationships" or "attributable material relationships." Will broadening these newly adopted definitions of material relationships to include other types of financial or operational agreements further enhance the Commission's ability to achieve the statutory goals intended by Congress – namely ensuring that designated entities participate in the provision of spectrum-based services, and preventing unjust enrichment as a result of the methods employed to issue licenses?[186] If commenters support broadening the definitions of material relationships to include additional agreements, they should provide specific examples of the types of agreements or combinations of agreements that should fall within each definition as well as explanation of how including such agreements will achieve the Commission's statutory mandates. To the extent we decide to broaden the definitions of material relationships to include other types of agreements, should there be any difference in our assessment of such agreements when entered into by the designated entity with different classes of entities? For example, should our rules treat a designated entity's agreements with an existing licensee of CMRS spectrum differently than similar agreements with an investor that does not currently hold any licenses for CMRS spectrum? To the extent that commenters support such differential treatment, we request that they provide evidence supporting such action, including its relation to the designated entity program.

79. Should our concern regarding relationships between designated entity applicants or licensees and other entities differ depending upon the type of entity at issue and the circumstances surrounding the relationship? Should we reconsider adopting a minimum equity requirement for designated entity applicants or define material relationship in a way that would prohibit a designated entity applicant from securing all of its capitalization from outside sources? Should we adopt commenters' suggestions to include additional operational agreements in our definitions of material relationship or does doing so create technological and practical restrictions that could hinder a designated entity licensee's ability to become a provider of spectrum based services, as intended by Congress?

[185] *See, e.g.,* Comments of CTIA at 2 ("the Notice proposes to embark on a path that does not address the problems it purports to fix."); Comments of Dobson at 3 ("there is nothing in the FNPRM that suggests that the concerns that Council Tree has expressed would be ameliorated by applying the proposed restriction only to one group of strategic investors and not another."); Comments of Verizon Wireless at 1-2 ("If the Commission feels compelled to make changes it should do so more broadly and effectively restrict investment from all companies that with revenues greater than $125 million."); Comments of U.S. Wirefree at 11 ("There is no rational basis for discriminating against carrier investment in a DE based solely on the size of the carrier. . . . If the Commission wants to restrain ownership in DEs by other wireless carriers it should apply this restraint uniformly."); Comments of Cook Inlet at 13 ("It is not clear how the incentives or practices of these carriers are any more detrimental to the program than the incentives of any investor in a designated entity, whether a large financial institution, venture capital fund, small wireless carrier or otherwise.").

[186] 47 U.S.C. §§ 309(j)(3)(B), 309(j)(4)(D)-(E).

80. Based on the limited record developed in response to the *Further Notice*, and our extensive experience in administering the designated entity program, we are concerned that additional types of relationships could have the potential to confer significant influence over the actions of a designated entity licensee thereby allowing an ineligible entity the ability to gain undue advantages in the communications marketplace through the benefits offered to a designated entity applicant. We therefore seek comment on the specific types of additional agreements that should fall within our definitions of "impermissible material relationships" and "attributable material relationships" so that we may be better able to prevent the potential for this type of abuse of the designated entity program, thereby ensuring the award of our designated entity benefits only to legitimate small businesses. Are the new rules we adopt today sufficient to safeguard against many of these concerns?

81. We generally do not have the same concerns regarding relationships between designated entity applicants and those who do not have interests in spectrum capacity or the provision of service, such as financial institutions or venture capital firms, provided that such entities do not have a controlling interest relationship with the applicant. Presumptively, for those entities, the overarching goal and primary incentive for partnering with a designated entity is to seek a return on investment rather than to provide service themselves using the designated entity's spectrum licenses. We seek comment on this presumption. Likewise, we presume that where an entity is not already providing communications services, there is no opportunity for it to bundle existing communications services with a strategic wireless partner, and there is less potential for those entities to exert undue influence over a designated entity licensee's decision making regarding its service provision or the use of its licensed spectrum. We seek comment on this presumption. Assuming that these presumptions are valid, we anticipate that such relationships do not require the additional safeguards we may apply to relationships with other entities that have differing incentives and motivations. For instance, if we included financial relationships in our definition of either "impermissible material relationships" or "attributable material relationship" we might specifically exclude relationships with financial institutions from such a definition. We seek comment on whether we should specifically do so.

82. With regard to financial relationships, should the Commission conclude that the greater the financial stake an entity has in a designated entity the more incentive it has to significantly influence the designated entity licensee's decisions regarding its provision of service? We also seek comment on whether we should expand our definitions of "impermissible material relationship" or "attributable material relationship" to include any financial relationship(s) (including any combination of equity, debt, loan or credit agreements, as well as future interests for such financial arrangements) between a designated entity applicant or licensee and another entity that represents more than a certain percentage of the designated entity's total financing. If so, what is the appropriate percentage? Council Tree suggested that a more than a 33 percent financial stake should be "material." Should such a financial interest be considered to be an "impermissible material relationship" or "attributable material relationship?" We note that the 33 percent benchmark offered by Council Tree is derived from the Commission's broadcast ownership attribution rules, but the relevance of that benchmark in this context is uncertain, given the different policy issues that were considered in adopting that percentage limitation in the broadcast context.[187] Other commenters suggested that our definition of material relationship should include as little as a percent financial interest or as much as a 50 percent interest. We seek comment on how the percentage of an entity's financial interest in a designated entity applicant or licensee should be considered in our definitions of "impermissible material relationship" or "attributable material relationship." We are concerned that we do not want to create a situation in which additional safeguards regarding financial interests render a designated entity without any avenues for access to much needed capital.

83. Additionally, are there circumstances in which we should agree with Council Tree and others that argue that the definition of material relationship should include, "without limitation,

[187] 47 C.F.R. § 73.3555.

management agreements, trademark license agreements, joint marketing agreements, future interest agreements (such as puts, calls, options, and warrants), and long-term *de facto* and spectrum manager leasing arrangements?"[188] If so, should such relationships be considered to be "impermissible material relationships" or "attributable material relationships?" Under what circumstances, does the existence of any agreement between a designated entity applicant or licensee and another entity have the strong potential to convey influence over the operations of the designated entity and the deployment of its spectrum in a manner contrary to that intended by Congress?

84. We also seek comment upon whether we should adopt even tighter safeguards to prevent the development of relationships that might deter designated entities from evolving into independent facilities-based competitors. For example, are there circumstances in which we should define "material relationship" to include "any relationship, financial and/or operational" between a designated entity applicant or licensee and another entity? For instance, does the likelihood that certain relationships will influence a designated entity's provision of service increase when agreements are entered into with an entity that has existing self interests in the same spectrum?

85. If we include all agreements, both financial and operational, as either "impermissible material relationships" or "attributable material relationships" between designated entities and entities that have existing spectrum interests in the same geographic areas can we reduce the reliance of designated entities on those that might provide funding or operational support in a manner designed to complement their own services rather than for facilitating the emergence of new technologies and new facilities-based competitors? In so doing, can we reduce the potential for abuse of the designated entity program and can we lessen the possibility of entities with existing self interests to use relationships with designated entities as a means to gain access to spectrum at a discounted value?

86. We seek comment on any and all of the agreements the Commission should consider including in its definitions of "impermissible material relationships" or "attributable material relationships" and whether the Commission should take into consideration whether such agreements are made with certain types of entities with certain geographic interests.

87. *Personal Net Worth*. We seek comment on whether we should include personal net worth in determining designated entity eligibility and if so, whether we should adopt the proposal put forth by Council Tree in its *ex parte* to prohibit individuals with a net worth of $3 million or more (excluding the value of a primary residence) from having a controlling interest in a designated entity[189] or whether we should place other net-worth-based restrictions on designated entity eligibility.

88. In its *ex parte*, Council Tree specifically urges the Commission to prohibit individuals with a net worth of $3 million or more (excluding the value of a primary residence) from having a controlling interest in a designated entity.[190] It argues that in the absence of a personal net worth

[188] A number of commenters also generally appeared to support the premise of Council Tree's proposals without specifically commenting on how the Commission might define "material relationship." *See e.g.*, Comments of MobiPCS at 1; Comments of Suncom at 1; Comments of USCC at 2-3, 5; Reply Comments of Royal Street at 1.

[189] Council Tree *ex parte* at 2, 6-7, 13.

[190] *Id*. Council Tree suggests that the Commission measure personal net worth as of the time of filing the applicant's short form application. Council Tree notes that this limitation should be applied only to an individual with *de jure* or *de facto* control of the applicant as determined under the Commission's controlling interest standard. It believes that such a condition is important because the Commission's attribution rules provide that the officers and directors of an applicant, and the officers and directors of an entity that control the applicant, shall be "considered" to have a controlling interest in the applicant. As such, Council Tree asserts that unless application of the personal net worth test is limited to individuals with actual *de jure* or *de facto* control of the applicant, legitimate designated entities would risk losing preference eligibility due to the net worth of an officer or director who has only constructive control under the Commission's rules, which could discourage designated entities from hiring experienced managers and industry veterans to serve as officers or directors.

limitation, there is very little to prevent wealthy individuals from seeking status as small businesses. According to Council Tree, designated entities "have come to be dominated by high net worth individuals, particularly well-connected former wireless industry executives who have no need for government assistance." Council Tree asserts that high net worth individuals have exploited the designated entity program since they recognize that the Commission does not count personal wealth in assessing the size of a business that applies for auction-related bidding credits or set asides. In its comments filed in this proceeding, Council Tree continues to urge the Commission to close the "loophole" that, it alleges, allows "high net worth individuals to take advantage of designated entity preferences."[191]

89. Few commenters in this proceeding addressed Council Tree's proposal to impose a net worth prohibition. Cook Inlet acknowledges Council Tree's concern that wealthy individuals may have the ability to obtain designated entity benefits.[192] Carroll Wireless, Aloha Partners and Poplar argue that the proposal is "both unnecessary and impractical," in view of the investment needed for wireless and the difficulty in measuring individual net worth.[193] Those commenters also all allege that a net worth cap on individuals is impractical because "it would seem to eliminate many entrepreneurs who have been successful in wireless to date – and are the ones who can make a DE program work."[194] RTG and Rural Carriers oppose Council Tree's net worth proposal on the ground that such a rule possibly would exclude family-owned, independent rural telephone companies and small businesses and most cooperative rural telephone companies.[195]

90. In previous circumstances, where the Commission was focused primarily on creating flexibility for designated entities to have access to capital, the Commission generally has not adopted personal net worth restrictions, including personal income and assets, for purposes of eligibility for designated entity provisions.[196] In that context, the Commission has observed, for example, that personal net worth limits are difficult to apply and enforce and may be easily manipulated.[197] The Commission also has explained that it did not believe that eliminating the personal net worth limits would facilitate significant encroachment by "deep pockets" that can be accessed by wealthy individuals through affiliated entities because, in those instances in which access to such resources would create an unfair advantage, the affiliation rules will continue to apply and require that such an entity's assets and revenues be included in determining an applicant's size. The Commission previously has explained that it believed that the affiliation rules make the personal net worth rules largely unnecessary because most wealthy individuals are likely to have their wealth closely tied to ownership of another business.[198]

91. In the *Further Notice*, we did not address Council Tree's personal net worth proposal substantively, noting that it had been rejected in a prior proceeding.[199] After further considering, however, our rule modifications that we are adopting in this *Second Report and Order*, the additional matters that we are addressing herein, as well as Council Tree's continued urging to include a net worth prohibition, we are persuaded that we should seek further comment on this issue. Accordingly, we seek comment on whether the Commission should reconsider its treatment of personal net worth in

[191] Council Tree Comments at 6.

[192] Comments of Cook Inlet at 14-15. *See* Cook Inlet *ex parte* filing, dated February 16, 2006.

[193] Comments of Aloha Partners at 5; Comments of Carroll Wireless at 7; Comments of Poplar at 4.

[194] *Id.*

[195] Comments of RTG at 5; Reply Comments of Rural Carriers at 5-6.

[196] *Competitive Bidding Fifth MO &O*, 10 FCC Rcd at 403.

[197] *Id.* at 421 ¶ 30.

[198] *Id.*

[199] *See Further Notice*, 21 FCC Rcd at 1756-57 ¶ 5, n.17.

determining eligibility for designated entity benefits and if so, what changes the Commission should adopt and why. We specifically seek comment on Council Tree's proposal to prohibit individuals with a net worth of $3 million or more (excluding the value of a primary residence) from having a controlling interest. We ask commenters to address the validity of Council Tree's arguments in support of its proposal[200] and, if possible, to cite specific instances that may be relevant to evaluating the proposal of Council Tree or other proposals offered by commenters. We particularly seek comments on Council Tree's assertion that "an individual who has made a fortune in the wireless industry, but who is no longer affiliated with his or her former company, may form a new limited liability company . . .[,] use his or her contacts to partner with an existing wireless service provider" and then pledge his or her personal assets to secure financing for any desired capital contribution to the new entity.[201]

92. In addition to requesting comments on Council tree's proposal, we also ask commenters to propose any other individual net worth restrictions that they may deem necessary or appropriate to strengthen our rules. We also ask commenters supporting additional restrictions to discuss how such restrictions should be implemented? For example, should the attribution rules be amended with respect to the exclusion of personal income, or would any adopted restriction be more effectively implemented through some other rule? If commenters believe that no changes are needed in the Commission's current exclusion of individual net worth in determining designated entity eligibility, we ask that they explain their position in detail and include a discussion of whether they believe that the Commission should be concerned about the types of individuals described by Council Tree receiving benefiting from the designated entity program and, if not, why not. We ask that all commenters explain how the position that they advocate is consistent with the Commission's statutory responsibilities toward designated entities. In that regard, we seek comment on whether the potential threat, if any that an individual with sufficient wealth poses to the designated entity program is similar in nature to, or different from, the other threats that we address or raise as possibilities elsewhere in this *Second Report and Order*. We ask that commenters explain what they believe the similarities or differences are and how those factors should affect any actions by the Commission.

V. CONCLUSION

93. For all of the reasons set forth above, we modify our rules for determining the eligibility of applicants for size-based benefits in the context of competitive bidding and issue a *Second Notice of Proposed Rule Making* to consider whether we should adopt additional restrictions to further safeguard the benefits reserved for designated entities.

VI. PROCEDURAL MATTERS

A. Regulatory Flexibility Analyses

94. As required by the Regulatory Flexibility Act, *see* 5 U.S.C. § 604, the Commission has prepared a Final Regulatory Flexibility Analysis, set forth below at Appendix C.

95. An Initial Regulatory Flexibility Analysis ("IRFA") for the *Second Further Notice* is attached at Appendix D.[202] Comments on the IRFA should be labeled as IRFA Comments, and should be submitted pursuant to the filing dates and procedures set forth below.

[200] Council Tree argues, for example, that if a high net worth individual does *not* have his or her wealth tied to ownership of other businesses or if such other businesses have few or no gross revenues, individuals who are not the intended beneficiaries of the designated entity program could receive designated entity benefits

[201] Council Tree *ex parte* at 11.

[202] *See* 5 U.S.C. § 603.

B. Comment Filing Procedures

96. Pursuant to sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R §§ 1.415, 1.419, interested parties may file comments on or before 60 days after publication in the Federal Register and may file reply comments on or before 90 days after publication in the Federal Register. All filings related to this Second Further Notice of Proposed Rule Making should refer to WT Docket No. 05-211. Comments may be filed using: (1) the Commission's Electronic Comment Filing System (ECFS), (2) the Federal Government's eRulemaking Portal, or (3) by filing paper copies. *See* Electronic Filing of Documents in Rule Making Proceedings, 63 FR 24121 (1998).

97. Electronic Filers: Comments may be filed electronically using the Internet by accessing the ECFS: http://www.fcc.gov/cgb/ecfs/ or the Federal eRulemaking Portal: http://www.regulations.gov. Filers should follow the instructions provided on the website for submitting comments. For ECFS filers, if multiple docket or rule making numbers appear in the caption of this proceeding, filers must transmit one electronic copy of the comments for each docket or rule making number referenced in the caption. In completing the transmittal screen, filers should include their full name, U.S. Postal Service mailing address, and the applicable docket or rule making number. Parties may also submit an electronic comment by Internet e-mail. To get filing instructions, filers should send an e-mail to ecfs@fcc.gov, and include the following words in the body of the message, "get form." A sample form and directions will be sent in response.

98. Paper Filers: Parties who choose to file by paper must file an original and four copies of each filing. Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail (although we continue to experience delays in receiving U.S. Postal Service mail). All filings must be addressed to the Commission's Secretary, Office of the Secretary, Federal Communications Commission.

- The Commission's contractor will receive hand-delivered or messenger-delivered paper filings for the Commission's Secretary at 236 Massachusetts Avenue, N.E., Suite 110, Washington, DC 20002. The filing hours at this location are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes must be disposed of *before* entering the building.
- Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743.
- U.S. Postal Service first-class, Express, and Priority mail should be addressed to 445 12th Street, SW, Washington DC 20554.

C. Paperwork Reduction Act Analysis

99. This *Second Report and Order* contains new or modified information collection requirements subject to the Paperwork Reduction Act of 1995 (PRA), Public Law 104-13. It has been submitted to the Office of Management and Budget (OMB) for review under Section 3507(d) of the PRA. OMB, the general public, and other Federal agencies are invited to comment on the new or modified information collection requirements contained in this proceeding. In addition, we note that pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, *see* 44 U.S.C. 3506(c)(4), we previously sought specific comment on how the Commission might "further reduce the information collection burden for small business concerns with fewer than 25 employees."

100. In this *Second Report and Order*, we have assessed the effects of our new restriction on the award of designated entity benefits where an applicant or licensee has agreements, which create a material relationship, with one or more other entities for the lease (under either spectrum manager or *de facto* transfer leasing arrangements) or resale (including under a wholesale arrangement) of a portion of its spectrum capacity. We find that the rule we adopt will best ensure that the Commission can continue to award designated entity benefits to entities that Congress intended. While the new rule may impose a

new information collection on small businesses, including those with fewer than 25 employees, we conclude that this information collection is necessary to ensure that the benefits of the Commission's designated entity program are reserved only for legitimate small businesses.

101. This *Second Further Notice* contains proposed new or modified information collection requirements. The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public and the Office of Management and Budget ("OMB") to comment on the information collection requirements contained in this document, as required by the Paperwork Reduction Act of 1995, Public Law 104-13. Public and agency comments are due 60 days after the date of publication in the Federal Register. Comments should address: (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology. In addition, pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, see 44 U.S.C. 3506(c)(4), we seek specific comment on how we might "further reduce the information collection burden for small business concerns with fewer than 25 employees."

D. Congressional Review Act

102. The Commission will include a copy of this *Second Report and Order* and *Second Further Notice* in a report it will send to Congress and the Government Accountability Office pursuant to the Congressional Review Act, *see* 5 U.S.C. 801(a)(1)(A).

E. Ordering Clauses

103. Accordingly, IT IS ORDERED that, pursuant to sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. sections 154(i), 303(r), and 309(j), this *Second Report and Order* is hereby ADOPTED and Part 1 of the Commission's rules, 47 C.F.R. Part 1, is AMENDED as set forth below in Appendix B, effective 30 days after publication in the Federal Register, except for the grandfathering provisions which are effective upon release.

104. IT IS FURTHER ORDERED that pursuant to sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. sections 154(i), 303(r), and 309(j), this *Second Further Notice of Proposed Rule Making* is HEREBY ADOPTED.

105. IT IS FURTHER ORDERED that, pursuant to 47 U.S.C. § 155(c) and 47 C.F.R. §§ 0.131(c) and 0.331, the Chief of the Wireless Telecommunications Bureau IS GRANTED DELEGATED AUTHORITY to prescribe and set forth procedures for the implementation of the provisions adopted herein.

106. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, SHALL SEND a copy of this *Second Report and Order* and *Second Further Notice*, including the Final Regulatory Flexibility Analysis and the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Marlene H. Dortch
Secretary

APPENDIX A

Commenters

Comments

1. Aloha Partners, L.P. (“Aloha”)
2. Antares, Inc. (“Antares”)
3. Carroll Wireless, L.P. (“Carroll Wireless”)
4. Centennial Communications Corp. (“Centennial”)
5. Columbia Capital LLC (“Columbia Capital”)
6. Communications Advisory Counsel (“CAC”)
7. Comscape Telecommunications, Inc. (“Comscape”)
8. Cook Inlet Region, Inc. (“Cook Inlet”)
9. Council Tree Communications, Inc. (“Council Tree”)
10. CTIA – The Wireless Association (“CTIA”)
11. Dobson Communications Corporation (“Dobson”)
12. Doyon Communications, Inc. (“Doyon”)
13. Dull, Arvin D.
14. John Staurulakis, Inc.
15. Leap Wireless International, Inc. (“Leap”)
16. Madison Dearborn Partners, LLC (“Madison Dearborn”)
17. MetroPCS Communications, Inc. (“MetroPCS”)
18. Minority Media and Telecommunications Council (“MMTC”)
19. MobiPCS
20. National Association of Broadcasters (“NAB”)
21. National Hispanic Media Coalition (“NHMC”)
22. National Telecommunications Cooperative Association (“NTCA”)
23. NTCH, Inc.
24. NTCH, Inc, dba Clear Talk (“Clear Talk”)
25. Paging Systems, Inc. (“Paging Systems”)
26. Patrick, Levi
27. Poplar Associates, LLC (“Poplar”)
28. Rural Telecommunications Group, Inc. (“RTG”)
29. STX Wireless, LLC (“STX”)
30. Suncom Wireless, Inc. (“Suncom”)
31. T-Mobile USA, Inc. (“T-Mobile”)
32. United States Cellular Corporation (“USCC”)
33. U.S. Wirefree
34. Verizon Wireless (“Verizon Wireless”)
35. Wirefree Partners III, LLC (“Wirefree Partners”)
36. Wireless Broadband Service Providers Association (“WBSPA”)
37. Wireless Communications Association International, Inc. (“WCAI”)

Reply Comments

1. Antares, Inc. (“Antares”)
2. Blooston Rural De Colalition (“Blooston”)
3. Cablevision Systems Corporation (“CSC”)
4. Cingular Wireless, LLC (“Cingular”)
5. Consumers Union
6. Cook Inlet Region, Inc. (“Cook Inlet”)
7. Council Tree Communications, Inc. (“Council Tree”)
8. Ericsson, Inc. (“Ericsson”)
9. Leap Wireless International, Inc. (“Leap”)
10. Minority Media and Telecommunications Council (“MMTC”)
11. Royal Street Communications, LLC (“Royal Street”)
12. Rural Carriers
13. T-Mobile USA, Inc. (“T-Mobile”)
14. United States Cellular Corporation (“USCC”)
15. U.S. Wirefree
16. Verizon Wireless (“Verizon Wireless”)
17. Wirefree Partners III, LLC (“Wirefree Partners”)
18. Wireless Broadband Service Providers Association (“WBSPA”)

Notice of *Ex Parte* Presentations

1. Carroll Wireless et al (“Carroll”)
2. Cook Inlet Region, Inc. (“Cook Inlet”) *
3. Council Tree Communications, Inc. (“Council Tree”) *
4. CTIA – The Wireless Association (“CTIA”)
5. Doyon Communications, Inc. (“Doyon”)
6. Madison Dearborn Partners, LLC (“Madison Dearborn”)
7. Media Access Project (“MAP”)*
8. MetroPCS Communications, Inc. (“MetroPCS”)*
9. Minority Media and Telecommunications Council (“MMTC”)
10. National Hispanic Media Coalition (“NHMC”)*
11. National Telecommunications Cooperative Association (“NTCA”)*
12. Royal Street Communications, LLC (“Royal Street”)
13. T-Mobile USA, Inc. (“T-Mobile”)*
14. Transactional Transparency and Related Outreach Subcommittee
15. U.S. Department of Justice
16. Verizon Wireless (“Verizon Wireless”)*
17. Wirefree Partners III, LLC (“Wirefree Partners”)

* Indicates that more than one *ex parte* submission was filed

APPENDIX B

Final Rules

PART 1 – PRACTICE AND PROCEDURE

For the reasons discussed in the preamble, the FCC amends parts 1 of the Code of Federal Regulations to read as follows:

1. The authority citation for part 1 is revised to read as follows:

Authority: 15 U.S.C. 79 et seq.; 47 U.S.C. 151, 154(i), 154(j), 155, 157, 225, 303(r), and 309.

2. In § 1.913, paragraph (a) introductory text and the first sentence of paragraph (b) are revised and paragraph (a)(6) is added to read as follows:

§ 1.913 Application and notification forms; electronic and manual filing.

(a) Application and notification forms. Applicants, licensees, and spectrum lessees (see § 1.9003) shall use the following forms and associated schedules for all applications and notifications:

* * * * *

(6) FCC Form 609, Application to Report Eligibility Event. FCC Form 609 is used by licensees to apply for Commission approval of reportable eligibility events, as defined in § 1.2114.

(b) Electronic filing. Except as specified in paragraph (d) of this section or elsewhere in this chapter, all applications and other filings using the application and notification forms listed in this section or associated schedules must be filed electronically in accordance with the electronic filing instructions provided by ULS.

* * *

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3. Revise paragraph (b) introductory text and add paragraph (b)(5) to § 1.919 to read as follows:

§ 1.919 Ownership information.

* * * * *

(b) Any applicant or licensee that is subject to the reporting requirements of §1.2112 or § 1.2114 shall file an FCC Form 602, or file an updated form if the ownership information on a previously filed FCC Form

602 is not current, at the time it submits:

* * * * *

(5) An application reporting any reportable eligibility event, as defined in § 1.2114.

* * * * *

4. Revise paragraph (a)(2)(ii)(B) of § 1.2105 to read as follows:

§ 1.2105 Bidding application and certification procedures; prohibition of collusion.

(a) * * *

(2) * * *

(ii)(B) Applicant ownership and other information, as set forth in 1.2112.

* * * * *

5. In paragraph § 1.2110, paragraphs (b)(1)(i)-(ii) and (j) are revised , paragraphs (n) and (o) are redesignated as paragraphs (o) and (p), and paragraphs (b)(3)(iv) and (n) are added to read as follows:

§ 1.2110 Designated entities.

* * * * *

(b) * * *

(1) Size attribution.

(i) The gross revenues of the applicant (or licensee), its affiliates, its controlling interests, the affiliates of its controlling interests, and the entities with which it has an attributable material relationship shall be attributed to the applicant (or licensee) and considered on a cumulative basis and aggregated for purposes of determining whether the applicant (or licensee) is eligible for status as a small business, very small business, or entrepreneur, as those terms are defined in the service-specific rules. An applicant seeking status as a small business, very small business, or entrepreneur, as those terms are defined in the service-specific rules, must disclose on its short- and long-form applications, separately and in the aggregate, the gross revenues for each of the previous three years of the applicant (or licensee), its affiliates, its controlling interests, the affiliates of its controlling interests, and the entities with which it has an attributable material relationship.

(ii) If applicable, pursuant to § 24.709, the total assets of the applicant (or licensee), its affiliates, its

controlling interests, the affiliates of its controlling interests, and the entities with which it has an attributable material relationship shall be attributed to the applicant (or licensee) and considered on a cumulative basis and aggregated for purposes of determining whether the applicant (or licensee) is eligible for status as an entrepreneur. An applicant seeking status as an entrepreneur must disclose on its short- and long-form applications, separately and in the aggregate, the gross revenues for each of the previous two years of the applicant (or licensee), its affiliates, its controlling interests, the affiliates of its controlling interests, and the entities with which it has an attributable material relationship.

* * * * *

(3) * * *

(iv) Applicants or licensees with material relationships.

(A) Impermissible material relationships. An applicant or licensee that would otherwise be eligible for designated entity benefits under this section and applicable service-specific rules shall be ineligible for such benefits if the applicant or licensee has an impermissible material relationship. An applicant or licensee has an impermissible material relationship when it has arrangements with one or more entities for the lease or resale (including under a wholesale agreement) of, on a cumulative basis, more than 50 percent of the spectrum capacity of any one of the applicant's or licensee's licenses.

(B) Attributable material relationships. An applicant or licensee must attribute the gross revenues (and, if applicable, the total assets) of any entity, (including the controlling interests, affiliates, and affiliates of the controlling interests of that entity) with which the applicant or licensee has an attributable material relationship. An applicant or licensee has an attributable material relationship when it has one or more arrangements with any individual entity for the lease or resale (including under a wholesale agreement) of, on a cumulative basis, more than 25 percent of the spectrum capacity of any one of the applicant's or licensee's licenses.

(C) Grandfathering.

(1) Licensees. An impermissible or attributable material relationship shall not disqualify a licensee for previously awarded benefits with respect to a license awarded before April 25, 2006, based on spectrum

lease or resale (including wholesale) arrangements entered into before April 25, 2006.

(2) Applicants. An impermissible or attributable material relationship shall not disqualify an applicant seeking eligibility in an application for a license, authorization, assignment, or transfer of control or for partitioning or disaggregation filed before April 25, 2006, based on spectrum lease or resale (including wholesale) arrangements entered into before April 25, 2006. Any applicant seeking eligibility in an application for a license, authorization, assignment, or transfer of control or for partitioning or disaggregation filed after April 25, 2006, or in an application to participate in an auction in which bidding begins on or after [30 days after Federal Register publication], need not attribute the material relationship(s) of those entities that are its affiliates based solely on section 1.2110(c)(5)(i)(C) if those affiliates entered into such material relationship(s) before April 25, 2006, and are subject to a contractual prohibition preventing them from contributing to the applicant's total financing.

Example to paragraph (C)(2): Newco is an applicant seeking designated entity status in an auction in which bidding begins after the effective date of the rules. Investor is a controlling interest of Newco. Investor also is a controlling interest of Existing DE. Existing DE previously was awarded designated entity benefits and has impermissible material relationships based on leasing agreements entered into before April 25, 2006, with a third party, Lessee, that were in compliance with the Commission's designated eligibility standards prior to April 25, 2006,. In this example, Newco would not be prohibited from acquiring designated entity benefits solely because of the existing impermissible material relationships of its affiliate, Existing DE. Newco, Investor, and Existing DE, however, would need to enter into a contractual prohibition that prevents Existing DE from contributing to the total financing of Newco.

* * * * *

(j) Designated entities must describe on their long-form applications how they satisfy the requirements for eligibility for designated entity status, and must list and summarize on their long-form applications all agreements that affect designated entity status such as partnership agreements, shareholder agreements, management agreements, spectrum leasing arrangements, spectrum resale (including wholesale) arrangements, and all other agreements, including oral agreements, establishing, as applicable, de facto or de

jure control of the entity or the presence or absence of impermissible and attributable material relationships. Designated entities also must provide the date(s) on which they entered into each of the agreements listed. In addition, designated entities must file with their long-form applications a copy of each such agreement. In order to enable the Commission to audit designated entity eligibility on an ongoing basis, designated entities that are awarded eligibility must, for the term of the license, maintain at their facilities or with their designated agents the lists, summaries, dates, and copies of agreements required to be identified and provided to the Commission pursuant to this paragraph and to § 1.2114.

* * * * *

(n) Annual reports. Each designated entity licensee must file with the Commission an annual report within five business days before the anniversary date of the designated entity's license grant. The annual report shall include, at a minimum, a list and summaries of all agreements and arrangements (including proposed agreements and arrangements) that relate to eligibility for designated entity benefits. In addition to a summary of each agreement or arrangement, this list must include the parties (including affiliates, controlling interests, and affiliates of controlling interests) to each agreement or arrangement, as well as the dates on which the parties entered into each agreement or arrangement. Annual reports will be filed no later than, and up to five business days before, the anniversary of the designated entity's license grant.

(o) Gross revenues. * * *

(p) Total assets. * * *

6. Revise paragraphs (a), (b) introductory text, the first sentence of paragraph (c)(2), the first sentence of paragraph (c)(3), (d)(1), and (d)(2) of § 1.2111 to read as follows:

§ 1.2111 Assignment or transfer of control: unjust enrichment.

(a) Reporting requirement. An applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of a license within three years of receiving a new license through a competitive bidding procedure must, together with its application for transfer of control or assignment, file with the Commission's statement indicating that its license was obtained through competitive bidding. Such applicant must also file with the Commission the associated contracts for sale, option agreements,

management agreements, or other documents disclosing the local consideration that the applicant would receive in return for the transfer or assignment of its license (see § 1.948). This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below market financing).

(b) Unjust enrichment payment: set-aside. As specified in this paragraph an applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of, or for entry into a material relationship (see §§ 1.2110, 1.2114) (otherwise permitted under the Commission's rules) involving, a license acquired by the applicant pursuant to a set-aside for eligible designated entities under § 1.2110(c), or which proposes to take any other action relating to ownership or control that will result in loss of eligibility as a designated entity, must seek Commission approval and may be required to make an unjust enrichment payment (Payment) to the Commission by cashier's check or wire transfer before consent will be granted. The Payment will be based upon a schedule that will take account of the term of the license, any applicable construction benchmarks, and the estimated value of the set-aside benefit, which will be calculated as the difference between the amount paid by the designated entity for the license and the value of comparable non-set-aside license in the free market at the time of the auction. The Commission will establish the amount of the Payment and the burden will be on the applicants to disprove this amount. No payment will be required if:

* * *

(c) * * *

(2) If a licensee that utilizes installment financing under this section seeks to make any change in ownership structure or to enter into a material relationship (see § 1.2110) that would result in the licensee losing eligibility for installment payments, the licensee shall first seek Commission approval and must make full payment of the remaining unpaid principal and any unpaid interest accrued through the date of such change as a condition of approval. * * *

(3) If a licensee seeks to make any change in ownership or to enter into a material relationship (see § 1.2110) that would result in the licensee qualifying for a less favorable installment plan under this section,

the licensee shall seek Commission approval and must adjust its payment plan to reflect its new eligibility status. * * *

(d) * * *

(1) A licensee that utilizes a bidding credit, and that during the initial term seeks to assign or transfer control of a license to an entity that does not meet the eligibility criteria for a bidding credit, will be required to reimburse the U.S. Government for the amount of the bidding credit, plus interest based on the rate for ten year U.S. Treasury obligations applicable on the date the license was granted, as a condition of Commission approval of the assignment or transfer. If, within the initial term of the license, a licensee that utilizes a bidding credit seeks to assign or transfer control of a license to an entity that is eligible for a lower bidding credit, the difference between the bidding credit obtained by the assigning party and the bidding credit for which the acquiring party would qualify, plus interest based on the rate for ten year U.S. treasury obligations applicable on the date the license is granted, must be paid to the U.S. Government as a condition of Commission approval of the assignment or transfer. If, within the initial term of the license, a licensee that utilizes a bidding credit seeks to make any ownership change or to enter into a material relationship (see § 1.2110) that would result in the licensee losing eligibility for a bidding credit (or qualifying for a lower bidding credit), the amount of the bidding credit (or the difference between the bidding credit originally obtained and the bidding credit for which the licensee would qualify after restructuring or entry into a material relationship), plus interest based on the rate for ten year U.S. treasury obligations applicable on the date the license is granted, must be paid to the U.S. Government as a condition of Commission approval of the assignment or transfer or of a reportable eligibility event (see § 1.2114).

(2) Payment schedule.

(i) The amount of payments made pursuant to paragraph (d)(1) of this section will be 100 percent of the value of the bidding credit prior to the filing of the notification informing the Commission that the construction requirements applicable at the end of the initial license term have been met. If the notification informing the Commission that the construction requirements applicable at the end of the initial license term have been met, the amount of the payments will be reduced over time as follows:

(A) A loss of eligibility in the first five years of the license term will result in a forfeiture of 100 percent of the value of the bidding credit (or in the case of eligibility changing to qualify for a lower bidding credit, 100 percent of the difference between the bidding credit received and the bidding credit for which it is eligible);

(B) A loss of eligibility in years 6 and 7 of the license term will result in a forfeiture of 75 percent of the value of the bidding credit (or in the case of eligibility changing to qualify for a lower bidding credit, 75 percent of the difference between the bidding credit received and the bidding credit for which it is eligible);

(C) A loss of eligibility in years 8 and 9 of the license term will result in a forfeiture of 50 percent of the value of the bidding credit (or in the case of eligibility changing to qualify for a lower bidding credit, 50 percent of the difference between the bidding credit received and the bidding credit for which it is eligible); and

(D) A loss of eligibility in year 10 of the license term will result in a forfeiture of 25 percent of the value of the bidding credit (or in the case of eligibility changing to qualify for a lower bidding credit, 25 percent of the difference between the bidding credit received and the bidding credit for which it is eligible).

(ii) These payments will have to be paid to the United States Treasury as a condition of approval of the assignment, transfer, ownership change, or reportable eligibility event (see §1.2114).

* * * * *

7. In § 1.2112, add new paragraphs (b)(1)(iii) and (b)(2)(vii), redesignate paragraph (b)(1)(iii) as (b)(1)(iv), and revise redesignated paragraph (b)(1)(iv) and paragraphs (b)(2)(iii) and (v) of to read as follows:

§ 1.2112 Ownership disclosure requirements for applications.

* * * * *

(b) * * *

(1) * * *

(iii) List all parties with which the applicant has entered into arrangements for the spectrum lease or resale (including wholesale agreements) of any of the capacity of any of the applicant's spectrum.

(iv) List separately and in the aggregate the gross revenues, computed in accordance with § 1.2110, for each of the following: The applicant, its affiliates, its controlling interests, the affiliates of its controlling interests, and the entities with which it has an attributable material relationship; and if a consortium of small businesses, the members comprising the consortium.

* * * * *

(2) * * *

(iii) List and summarize all agreements or instruments (with appropriate references to specific provisions in the text of such agreements and instruments) that support the applicant's eligibility as a small business under the applicable designated entity provisions, including the establishment of de facto or de jure control or the presence or absence of impermissible and attributable material relationships. Such agreements and instruments include articles of incorporation and bylaws, partnership agreements, shareholder agreements, voting or other trust agreements, management agreements, franchise agreements, spectrum leasing arrangements, spectrum resale (including wholesale) arrangements, and any other relevant agreements (including letters of intent), oral or written;

(iv) * * *

(v) List separately and in the aggregate the gross revenues, computed in accordance with § 1.2110, for each of the following: the applicant, its affiliates, its controlling interests, affiliates of its controlling interests, and parties with which it has attributable material relationships; and if a consortium of small businesses, the members comprising the consortium; and

(vi) * * *

(vii) List and summarize any agreements in which the applicant has entered into arrangements for the lease or resale (including wholesale agreements) of any of the spectrum capacity of the license that is the subject of the application.

8. Add new section 1.2114 to read as follows:

§ 1.2114 Reporting of Eligibility Event.

(a) A designated entity must seek Commission approval for all reportable eligibility events. A reportable

eligibility event is:

(1) Any spectrum lease (as defined in § 1.9003) or resale arrangement (including wholesale agreements) with one entity or on a cumulative basis that would cause a licensee to lose eligibility for installment payments, a set-aside license, or a bidding credit (or for a particular level of bidding credit) under § 1.2110 and applicable service-specific rules.

(2) Any other event that would lead to a change in the eligibility of a licensee for designated entity benefits.

(b) Documents listed on and filed with application. A designated entity filing an application pursuant to this section must –

(1) List and summarize on the application all agreements and arrangements (including proposed agreements and arrangements) that give rise to or otherwise relate to a reportable eligibility event. In addition to a summary of each agreement or arrangement, this list must include the parties (including each party's affiliates, its controlling interests, the affiliates of its controlling interests, its spectrum lessees, and its spectrum resellers and wholesalers) to each agreement or arrangement, as well as the dates on which the parties entered into each agreement or arrangement.

(2) File with the application a copy of each agreement and arrangement listed pursuant to this paragraph.

(3) Maintain at its facilities or with its designated agents, for the term of the license, the lists, summaries, dates, and copies of agreements and arrangements required to be provided to the Commission pursuant to this section.

(c) Application fees. The application reporting the eligibility event will be treated as a transfer of control for purposes of determining the applicable application fees as set forth in § 1.1102.

(d) Streamlined approval procedures.

(1) The eligibility event application will be placed on public notice once the application is sufficiently complete and accepted for filing (see § 1.933).

(2) Petitions to deny filed in accordance with § 309(d) of the Communications Act must comply with the provisions of § 1.939, except that such petitions must be filed no later than 14 days following the date of the Public Notice listing the application as accepted for filing.

(3) No later than 21 days following the date of the Public Notice listing an application as accepted for filing, the Wireless Telecommunications Bureau (Bureau) will grant the application, deny the application, or remove the application from streamlined processing for further review.

(4) Grant of the application will be reflected in a Public Notice (see § 1.933(a)(2)) promptly issued after the grant.

(5) If the Bureau determines to remove an application from streamlined processing, it will issue a Public Notice indicating that the application has been removed from streamlined processing. Within 90 days of that Public Notice, the Bureau will either take action upon the application or provide public notice that an additional 90-day period for review is needed.

(e) Public notice of application. Applications under this subpart will be placed on an informational public notice on a weekly basis (see § 1.933(a)).

(f) Contents of the application. The application must contain all information requested on the applicable form, any additional information and certifications required by the rules in this chapter, and any rules pertaining to the specific service for which the application is filed.

(g) The designated entity is required to update any change in a relationship that gave rise to a reportable eligibility event.

APPENDIX C

Final Regulatory Flexibility Analysis

As required by the Regulatory Flexibility Act (RFA),[203] an Initial Regulatory Flexibility Analysis (IRFA) was incorporated into the Further Notice of Proposed Rule Making ("*Further Notice*") in WT Docket No. 05-211. The Commission sought written public comment in the Further Notice on possible changes to its competitive bidding rules, as well as on the IRFA.[204] One commenter addressed the IRFA. This Final Regulatory Flexibility Analysis conforms to the IRFA.[205]

A. Need for, and Objectives of, the Second Report and Order

This *Second Report and Order* adopts modifications to the Commission's rules for determining the eligibility of applicants for size-based benefits in the context of competitive bidding. Over the last decade, the Commission has engaged in numerous rulemakings and adjudicatory investigations to prevent companies from circumventing the objectives of the designated entity eligibility rules.[206] To that end, in determining whether to award designated entity benefits, the Commission adopted a strict eligibility standard that focused on whether the applicant maintained control of the corporate entity.[207] The Commission's objective in employing such a standard was "to deter the establishment of sham companies in a manner that permits easy resolution of eligibility issues without the delay of administrative hearings."[208] The Commission intends its small business provisions to be available only to bona fide small businesses.

Consequently, the rules as modified by the *Second Report and Order* provide that certain material relationships of an applicant for designated entity benefits will be a factor in determining the applicant's eligibility. The *Second Report and Order* provides that if an applicant or licensee has agreements that together enable it to lease or resell more than 50 percent of the spectrum capacity of any individual licenses, the applicant or licensee will be ineligible for designated entity benefits. Further, the *Second Report and Order* also provides that if an applicant or licensee has agreements with any other entity, including entities or individuals attributable to that other entity that enable the applicant or licensee to lease or resell more than 25 percent of the spectrum capacity of any individual licenses, the other entity will be attributed to the applicant or licensee when determining the applicant's or licensee's eligibility for designated entity benefits. Finally, the modifications of the *Second Report and Order* strengthen the Commission's unjust enrichment rules to better deter attempts at circumvention and to recapture designated entity benefits when there has been a change in eligibility on a license-by-license basis. Similarly, to ensure our continued ability to safeguard the award of designated entity benefits, we provide

[203] *See generally* 5 U.S.C. § 603. The RFA, *see* 5 U.S.C. §§ 601 – 612, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

[204] Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, WT Docket No. 05-211, *Further Notice of Proposed Rule Making*, 21 FCC Rcd 1753 (2006), 71 FR 6992 (February 10, 2006).

[205] *See generally* 5 U.S.C. § 604.

[206] *See, e.g., Competitive Bidding Second Report and Order,* 9 FCC Rcd 2348 (1994); *Part 1 Fifth Report and Order*, 15 FCC Rcd 15293 (2000); Application of ClearComm, L.P., *Memorandum Opinion and Order*, 16 FCC Rcd 18627 (2001).

[207] *Competitive Bidding Second Report and Order*, 9 FCC Rcd at 2396, ¶ 277.

[208] *Id.* at 2397 ¶ 278.

clarification regarding how the Commission will implement its rules concerning audits and we refine our rules with respect to the reporting obligations of designated entities.

These rule modifications will enhance the Commission's ability to carry out Congress's statutory plan in accordance with the intent of Congress that every recipient of designated entity benefits uses its licenses directly to provide facilities-based telecommunications services for the benefit of the public. In making these changes to the rules, the Commission takes another important step in fulfilling its statutory mandate to facilitate the participation of small businesses in the provision of spectrum based services.[209]

B. Summary of Significant Issues Raised By Public Comment in Response to the IRFA

The National Telecommunications Cooperative Association filed comments in response to the IRFA stating, among other things, that the Commission must take steps to minimize the economic impact of its proposed rules on small entities. NTCA asserts that the Commission must tailor its rules narrowly enough to target only real abuse, rather than capturing all rural telephone companies with any ties to a large in-region wireless provider, or it should exempt rural telephone companies from the rules' provision.[210]

C. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply

The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.[211] The RFA generally defines the term "small entity" as having the same meaning as the terms "small organization," "small business," and "small governmental jurisdiction."[212] The term "small business" has the same meaning as the term "small business concern" under the Small Business Act.[213] A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the SBA.

A small organization is generally "any not-for-profit enterprise which is independently owned and operated and is not dominant in its field."[214] Nationwide, as of 2002, there were approximately 1.6 million small organizations.[215] The term "small governmental jurisdiction" is defined generally as "governments of cities, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand."[216] Census Bureau data for 2002 indicate that there were 87,525 local governmental jurisdictions in the United States.[217] We estimate that, of this total, 84,377 entities were

[209] 47 U.S.C. §309(j)(4)(D).

[210] Comments of NTCA at 9.

[211] 5 U.S.C. § 603(b)(3).

[212] *Id.* § 601(6).

[213] *Id.* § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). Pursuant to the RFA, the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register." *Id.* § 601(3).

[214] *Id.* § 601(4).

[215] Independent Sector, The New Nonprofit Almanac & Desk Reference (2002).

[216] 5 U.S.C. § 601(5).

[217] U.S. Census Bureau, Statistical Abstract of the United States: 2006, Section 8, page 272, Table 415.

"small governmental jurisdictions."[218] Thus, we estimate that most governmental jurisdictions are small. Nationwide, there are a total of approximately 22.4 million small businesses, according to SBA data.[219]

The changes and additions to the Commission's rules adopted in the *Second Report and Order* are of general applicability to all services, applying to all entities of any size that seek eligibility to participate in Commission auctions as a designated entity and/or that hold licenses won through competitive bidding that are subject to designated entity benefits. Accordingly, this FRFA provides a general analysis of the impact of the proposals on small businesses rather than a service by service analysis. The number of entities that may apply to participate in future Commission auctions is unknown. The number of small businesses that have participated in prior auctions has varied. In all of our auctions held to date, 1,975 out of a total of 3,545 qualified bidders either have claimed eligibility for small business bidding credits or have self-reported their status as small businesses as that term has been defined under rules adopted by the Commission for specific services.[220] In addition, we note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of changes in control, changes in material relationships or assignments or transfers, unjust enrichment issues are implicated.

D. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements

The Commission will require additional information from applicants in order to ensure compliance with the policies and rules adopted by the *Second Report and Order*. For example, designated entity applicants that have filed applications to participate in an auction for which bidding will begin on or after the effective date of the rules, will be required to amend their applications on or after the effective date of the rule changes with a statement declaring, under penalty of perjury, that the applicant is qualified as a designated entity pursuant to the Commission's rules effective as of the date of the statement. In addition, the Commission adopts rules to make modifications, as necessary, to FCC forms related to auction, licensing, and leasing applications. Specifically, the modifications will require that designated entities report any relevant material relationship(s), as defined in newly adopted sections of 1.2110, reached after the date the rules are published in the Federal Register, even if the material relationship between the designated entity and the other entity would not have triggered a reporting requirement under the rules prior to this *Second Report and Order*.[221]

[218] We assume that the villages, school districts, and special districts are small, and total 48,558. *See* U.S. Census Bureau, Statistical Abstract of the United States: 2006, section 8, page 273, Table 417. For 2002, Census Bureau data indicate that the total number of county, municipal, and township governments nationwide was 38,967, of which 35,819 were small. *Id.*

[219] *See* SBA, Programs and Services, SBA Pamphlet No. CO-0028, at page 40 (July 2002).

[220] This figure is as of March 29, 2006.

[221] *See generally* 47 C.F.R. §§ 1.948, 1.9020(i), 1.9030(h), (i).

E. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): "(1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the rule or any part thereof for small entities."[222]

The *Further Notice* sought comment on several options for modifying its designated entity eligibility rules and specifically sought comment from small entities. The options included various ways to consider whether the Commission should award designated entity benefits where an applicant for such benefits also had financial or operational agreements with a larger entity. In considering these options, for the purposes of determining designated entity eligibility, the Commission defined the effect of entering certain agreements. By adopting the rules in the *Second Report and Order,* the Commission will enhance its ability to carry out Congress's statutory plan that every recipient of designated entity benefits uses their licenses directly to provide facilities-based telecommunications services, for the benefit of the public.

F. Report to Congress

The Commission will send a copy of the *Second Report and Order*, including this FRFA, in a report to be sent to Congress pursuant to the SBREFA.[223] In addition, the Commission will send a copy of the *Second Report and Order*, including the FRFA, to the Chief Counsel for Advocacy of the SBA. A copy of the *Second Report and Order* and the FRFA (or summaries thereof) will also be published in the Federal Register.

[222] *See* 5 U.S.C. § 603.

[223] *See id.* § 801(a)(1)(A).

APPENDIX D

Initial Regulatory Flexibility Analysis

As required by the Regulatory Flexibility Act (RFA),[224] the Commission has prepared this Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on small entities by the policies and rules proposed in the *Second Further Notice of Proposed Rule Making* ("*Second Further Notice*"). Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments provided in this *Second Further Notice*. The Commission will send a copy of the *Second Further Notice*, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration (SBA).[225] In addition, the *Second Further Notice* and the IRFA (or summaries thereof) will be published in the Federal Register.[226]

A. Need for, and Objectives of, the Proposed Rules

The initial *Further Notice* in this proceeding tentatively concluded that it should restrict the award of designated entity benefits to an otherwise qualified applicant where it has a "material relationship" with a "large in-region incumbent wireless service provider." The Commission sought comment on how it should define the elements of such a restriction. Based on the Commission's experience in administering the designated entity program and the record developed in response to the *Further Notice*, this *Second Further Notice* seeks further comment on those issues, including comment to obtain additional economic evidence regarding how and under what circumstances an entity's size might affect its relationships and agreements with designated entity applicants and licensees. The *Second Further Notice* also seeks comment on whether the Commission should adopt additional rule changes that would restrict the award of designated entity benefits under certain circumstances and in connection with relationships with certain types of entities and individuals with high personal net worth, including whether and how in-region relationships and personal net worth should be considered in determining eligibility for designated entity benefits.

Over the last decade, the Commission has engaged in numerous rulemakings and adjudicatory investigations to prevent companies from circumventing the objectives of the designated entity eligibility rules.[227] To that end, in determining whether to award designated entity benefits, the Commission adopted a strict eligibility standard that focused on whether the applicant maintained control of the corporate entity.[228] The Commission's objective in employing such a standard was "to deter the establishment of sham companies in a manner that permits easy resolution of eligibility issues without the delay of administrative hearings."[229] The Commission intends its small business provisions to be available only to bona fide small businesses.

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[224] *See generally* 5 U.S.C. § 603. The RFA, *see* 5 U.S.C. §§ 601 – 612, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

[225] *See* 5 U.S.C. § 603(a).

[226] *See id.*

[227] *See, e.g., Competitive Bidding Second Report and Order,* 9 FCC Rcd 2348 (1994); *Part 1 Fifth Report and Order*, 15 FCC Rcd 15293 (2000); Application of ClearComm, L.P., *Memorandum Opinion and Order*, 16 FCC Rcd 18627 (2001).

[228] *Competitive Bidding Second Report and Order*, 9 FCC Rcd at 2396 ¶ 277.

[229] *Id.* at 2397 ¶ 278.

B. Legal Basis

The proposed actions are authorized under Sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. Sections 154(i), 303(r), and 309(j).

C. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply

The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.[230] The RFA generally defines the term "small entity" as having the same meaning as the terms "small organization," "small business," and "small governmental jurisdiction."[231] The term "small business" has the same meaning as the term "small business concern" under the Small Business Act.[232] A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the SBA.

A small organization is generally "any not-for-profit enterprise which is independently owned and operated and is not dominant in its field."[233] Nationwide, as of 2002, there were approximately 1.6 million small organizations.[234] The term "small governmental jurisdiction" is defined as "governments of cities, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand."[235] Census Bureau data for 2002 indicate that there were 87,525 local governmental jurisdictions in the United States.[236] We estimate that, of this total, 84,377 entities were "small governmental jurisdictions."[237] Thus, we estimate that most governmental jurisdictions are small. Nationwide, there are a total of approximately 22.4 million small businesses, according to SBA data.[238]

Any proposed changes or additions to the Commission's Part 1 rules that may be made as a result of the *Second Further Notice* would be of general applicability to all services, applying to all entities of any size that apply to participate in Commission auctions. Accordingly, this IRFA provides a general analysis of the impact of the proposals on small businesses rather than a service by service analysis. The number of entities that may apply to participate in future Commission auctions is unknown. The number of small businesses that have participated in prior auctions has varied. In all of our auctions held to date, 1,975 out of a total of 3,545 qualified bidders either have claimed eligibility for small business bidding credits or have self-reported their status as small businesses as that term has been defined under rules

[230] 5 U.S.C. § 603(b)(3).

[231] *Id.* § 601(6).

[232] *Id.* § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). Pursuant to the RFA, the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register." *Id.* § 601(3).

[233] *Id.* § 601(4).

[234] Independent Sector, The New Nonprofit Almanac & Desk Reference (2002).

[235] 5 U.S.C. § 601(5).

[236] U.S. Census Bureau, Statistical Abstract of the United States: 2006, Section 8, page 272, Table 415.

[237] We assume that the villages, school districts, and special districts are small, and total 48,558. *See* U.S. Census Bureau, Statistical Abstract of the United States: 2006, section 8, page 273, Table 417. For 2002, Census Bureau data indicate that the total number of county, municipal, and township governments nationwide was 38,967, of which 35,819 were small. *Id.*

[238] *See* SBA, Programs and Services, SBA Pamphlet No. CO-0028, at 40 (July 2002).

adopted by the Commission for specific services.[239] In addition, we note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of assignments or transfers, unjust enrichment issues are implicated.

D. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements

The Commission will not require additional reporting, recordkeeping or other compliance requirements pursuant to this *Second Further Notice*.

E. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule or any part thereof for small entities.[240]

The initial *Further Notice* in this proceeding tentatively concluded that it should restrict the award of designated entity benefits to an otherwise qualified applicant where it has a "material relationship" with a "large in-region incumbent wireless service provider." The Commission sought comment on how it should define the elements of such a restriction. Based on the Commission's experience in administering the designated entity program and the record developed in response to the *Further Notice*, this *Second Further Notice* seeks further comment on those issues, including comment to obtain additional economic evidence regarding how and under what circumstances an entity's size might affect its relationships and agreements with designated entity applicants and licensees. The *Second Further Notice* also seeks comment on whether the Commission should adopt additional rule changes that would restrict the award of designated entity benefits under certain circumstances and in connection with relationships with certain types of entities and individuals with high personal net worth, including whether and how in-region relationships and personal net worth should be considered in determining eligibility for designated entity benefits. The *Second Further Notice* seeks guidance from the industry on how it should define the elements of any restrictions it might adopt regarding the award of designated entity benefits. Small entity comments are specifically requested.

F. Federal Rules that May Duplicate, Overlap, or Conflict with the Proposed Rule

None.

[239] This figure is as of March 29, 2006.

[240] *See* 5 U.S.C. § 603.

STATEMENT OF CHAIRMAN KEVIN J. MARTIN

Re: Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, WT Docket No. 05-211, Second Report and Order and Second Further Notice of Proposed Rule Making.

We initiated this proceeding to examine our rules governing designated entities to better achieve the purpose of ensuring that small businesses have an opportunity to participate in the provision of spectrum-based services. Today's order adopts several measures to help accomplish that goal. Specifically, we strengthen our unjust enrichment and spectrum leasing rules for designated entities in order to provide additional incentives for small businesses receiving bidding credits to offer facilities-based service. We also further the integrity of the designated entity program by implementing random audits, additional document and transaction reviews, and periodic reporting. Together, these measures significantly strengthen the designated entity program.

In the further notice portion of this item, we ask whether additional safeguards are necessary to reduce the opportunity for manipulation of our rules governing the provision of bidding credits to small businesses. I look forward to working with my colleagues as we continue to develop the record in this proceeding.

STATEMENT OF
COMMISSIONER MICHAEL J. COPPS

Re: Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, WT Docket No. 05-211, Second Report and Order and Second Further Notice of Proposed Rule Making.

In this age when telecommunications companies seem only to grow larger and larger, it is important to have programs that encourage competition from smaller entrepreneurs. This is exactly what the Designated Entity (DE) program is all about and it is why we must do everything we can to make this program perform as intended. Small companies must have a fighting chance to compete with industry giants to obtain valuable spectrum. In an era of consolidation, the program is especially important to rural areas that might otherwise remain underserved. Quite frankly, rural America seems too often to have been pushed off the big companies' radar scopes. This is a central reason why I remain strongly committed to small carriers' participation in spectrum auctions. It is good policy; it also happens to be the law.

But let's be candid. Whenever government attempts to provide incentive programs for small business, there are those who try to twist the rules in order to gain unwarranted entry into these programs. We have seen this in many business sectors and we have unfortunately experienced such chicanery and cheating in telecom too. We must not allow the bad apple to spoil the bushel, however. Instead we need good rules to curb the chicanery. Recent experience teaches us that we must move quickly to curb abuses of the DE program. News reports indicate that, in prior auctions, entities with deep pockets helped themselves to discounts they were never meant to enjoy. This unacceptable behavior threatens the integrity of our auctions and, worse, it cheats consumers. It costs taxpayers millions of dollars in foregone revenue. It also means that spectrum goes to those most willing and able to manipulate the rules of the game, rather than to the entities Congress actually intended to benefit. And it denies consumers the benefits of new and all-too-rare competition. So, our job is to deny wealthy companies or individuals any opportunity to misuse the DE discount to outbid small carriers – the very carriers the DE program is meant to protect.

Today we take meaningful steps in the right direction. We do so in time to apply new rules to the large and important Advanced Wireless Services (AWS) auction scheduled for this summer. I am grateful to the Chairman for his role in moving this item along in time to have these rules apply to the AWS auction. And I am grateful to him and to my other colleagues for their support of strong measures to prevent fraud and unjust enrichment by those who would seek to abuse this valuable program. In particular, I am pleased that by strengthening our unjust enrichment rules we take away the incentive for speculators to try to masquerade as legitimate DEs. Under our new rules, bidders who benefit from the 25 percent discount must forfeit that discount if they then turn around and sell some or all of their license rights to someone else. By eliminating the payoff for this "flipping" of licenses, we discourage sham buyers from participating in the first place. And most importantly, we reserve the DE program for companies that actually intend to use their spectrum to serve customers.

I am also pleased that we commit to thoroughly review the application and all relevant documents for each and every winning bidder claiming DE status. Additionally, we pledge to audit every DE at least once during the initial license term. These are two important safeguards against sham bidders, and I am glad the Commission agreed to implement them as well.

There is more to do to ensure the ongoing integrity and credibility of the DE program. For instance, I have real questions about whether a company should be able to qualify for the DE discount if it is owned in large part by a multi-billion-dollar wireless company – or any multi-billion-dollar communications company, for that matter. I believe the unjust enrichment reforms we announce today

will go a long way towards eliminating the worst abuses of this kind. But we still need to consider whether additional partnership restrictions are warranted.

At the same time, we must also be cautious about overshooting the mark and harming the very small carriers and entrepreneurs that Congress meant to protect. Legitimate DEs must have access to capital to compete meaningfully against the large carriers. I would not support any measures that improperly compromised their ability to do so.

The limited time available to us for consideration of this item did not allow us to resolve these questions. I would have preferred launching this proceeding last summer so as to facilitate a more thorough review in time for comprehensive action today. But given the importance of both the upcoming AWS auction and the DE program, I think that the item we announce today is the most prudent course to protect the core values of the DE program. Certainly, we must be careful not to rush into further changes without full consideration of all their consequences, unintended as well as intended. I hope we will keep working on this program because another huge auction in the 700 MHz spectrum is not far off and we should have the program working as flawlessly as possible by then. In the meantime, I applaud the changes we make today to curb fraud and unjust enrichment and I thank my colleagues for their cooperative work to achieve these results.

STATEMENT OF
COMMISSIONER JONATHAN S. ADELSTEIN
APPROVING IN PART, DISSENTING IN PART

Re: Implementation of the Commercial Spectrum Enhancement Act and Modernization of the Commission's Competitive Bidding Rules and Procedures, WT Docket No. 05-211, Second Report and Order and Second Further Notice of Proposed Rule Making.

I must dissent from a large portion of this decision because it fails to accomplish the very specific goals the Commission outlined in the Further Notice and Proposed Rule Making (FNPRM) in this proceeding. While I endorse the narrow adjustments to the Designated Entity (DE) program that we adopt today, the majority falls far short of making the meaningful modifications to the DE program that were almost universally supported by commenters in this proceeding. I am disappointed that we were unable to follow through on our tentative conclusion from earlier this year, and believe that the Second FNPRM we adopt today is unnecessarily broad and complicated, and significantly ignores the full and complete record before us.

On January 27, 2006, my colleagues and I adopted an FNPRM in which we tentatively concluded that we should modify our Part 1 rules to restrict the award of designated entity benefits to an otherwise qualified designated entity where it has a "material relationship" with a "large in-region incumbent wireless service provider." This position was supported by a large and diverse group of commenters ranging from DEs[241] to Tier II carriers,[242] the minority community[243] to rural telephone companies,[244] and even members of Congress[245] and the Department of Justice.[246]

[241] "It is extremely positive and encouraging that the Commission has decided to take this opportunity to change its Designated Entity program rules so as to make available more fair and reasonable opportunities for bona fide designated entities to secure the critical spectrum necessary to compete in the face of ever-increasing industry consolidation dominated by large incumbent wireless service providers." Comments of STX Wireless, LLC.

[242] "It is not unreasonable or unfair for the Commission to update its designated entity program to take into account the greatly increased concentration of spectrum resources in the hands of the national wireless carriers. By limiting access of the national carriers to bid credit benefits, the Commission can effectively refocus its designated entity policies to expand opportunities for successful small business participation in the wireless industry." Reply Comments of United States Cellular Corporation at 2-3.

[243] "As carriers whose collective share of the wireless market is 89-90 percent, the five largest incumbents have the most to lose from the entry of facilities-based competitors into the wireless market, and therefore have the strongest incentives to manipulate the DE program in a manner that forestalls the competition that the DE program was meant to engender." Reply Comments of the Minority Media and Telecommunications Council (MMTC) at 3.

[244] "The Commission's tentative conclusion that it should modify its Part 1 rules to restrict the award of DE benefits such as bidding credits to an otherwise qualified DE where it has a 'material relationship' with a large, in-region incumbent wireless service provider is consistent with Section 309(j) of the Communications Act of 1934, as amended." Comments of The Rural Telecommunications Group, Inc. and The Organization for the Promotion and Advancement of Small Telecommunications Companies.

[245] "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." Letter from 10 Members of the Congressional Black Caucus to Chairman Kevin Martin (March 3, 2006).

[246] "The Department supports the Federal Communications Commission's proposal to deny designated entity benefits to entities that have a material relationship with a large in-region incumbent wireless service provider or a large entity that has a significant interest in communications services." *Ex Parte* Letter of the Department of Justice (March 17, 2006).

Yet, in a troubling and curious reversal, less than three months later, I stand alone in dissenting from our decision today to not to close this obvious loophole. It is stunning that we have failed to take any meaningful action to specifically address the single biggest issue facing the DE program given the overwhelming support in the record to do so. We missed a real opportunity to shut down what almost everyone recognizes has the potential for the largest abuse of our DE program: giant wireless companies using false fronts to get spectrum on the cheap.

During the past month, there has been considerable discussion about an alternative proposal to our original tentative conclusion – a limitation on investment in DEs by all providers of communications services over a given revenue threshold. While we do not vote on that proposal here, many commenters argued that this approach would not have tightened the DE program, but rather that the approach would have killed it. I certainly had concerns that the proposal, as structured, would have cast a wide net over the DE program – limiting funding to the DE community from almost all FCC-regulated companies, manufacturers, and service providers, whether circuit or IP-based. Not surprisingly, the proposal to adopt a low revenue threshold was loudly opposed by a number of significant voices including members of Congress,[247] two subcommittees of the FCC's own Advisory Committee on Diversity for Communications in the Digital Age,[248] current and former DEs,[249] and a quintet of Native Alaskan Corporation CEOs.[250] Some argue that so-called DE reform was really a disguise to eliminate an avenue of competition to incumbent wireless companies.[251]

Notwithstanding the flaws in this proposal, I have been willing to consider a variety of alternatives to our tentative conclusion that would have responded to complaints by large wireless carriers that they were being unfairly singled out or that we were ignoring our precedent of conducting market by market analyses in looking at spectrum issues. Moreover, if the wireless loophole was adequately addressed in a final decision, I was willing to consider a revenue-based restriction that affected all FCC regulatees provided that a revenue threshold was based on the record, not one that could indiscriminately shut down the DE program. But inexplicably, no deal could be struck. Ultimately, it was easier for the majority to make a few minor changes to the DE program than close the loophole that is recognized by almost everyone but this Commission.

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[247] "It would be wholly inconsistent with the promotion of these objectives for the Commission to limit the sources of capital and expertise available to new entrants in the complex wireless industry beyond the largest national carriers identified in the rulemaking who dominate the industry." Letter from Congressman Edolphus Towns and Congresswoman Diane Watson to Commissioners Michael Copps and Jonathan Adelstein (April 7, 2006).

[248] "The [Subcommittees] believe the Commission should receive the input of the full Committee before taking steps in response to the FNPRM released February 3, 2006 in WT Docket No. 05-211, recent reports regarding which suggest that the Commission may substantially undermine opportunities for diversity of ownership and other goals mandated by Section 309(j) of the Communications Act. Accordingly, the Subcommittee asks the Commission to convene the full Committee as soon as possible with respect to this matter." Statement of The Transactional Transparency and Related Outreach Subcommittee and the Career Advancement Subcommittee of the Advisory Committee on Diversity for Communications in the Digital Age (April 6, 2006).

[249] "Imposing severe new limitations on DEs sourcing investments from a broad category of companies defined as having revenues of $125 million or more will have the effect of killing the DE program." Ex Parte of Carroll Wireless, LP, CSM Wireless, LLC, Leap Wireless Int'l, Inc. United States Cellular Corp., TA Associates, 3G PCS, LLC, Royal Street Commc'ns, LLC, MetroPCS Commc'ns, Inc., Catalyst Investors and Council Tree Commc'ns, Inc. (April 5, 2006) ("Carroll Wireless et al").

[250] "Such ruling would effectively dismantle the DE Program as mandated by Congress. We urge the Commission to maintain the most important diversity tool at its disposal, stay with the clear record in this case and proceed with finalizing its Tentative Conclusion in this proceeding." Ex Parte of Doyon, Ltd., Koniag Development Corp., St. George Tanaq Corp. Chugach Alaska Corp., and Bethel Native Corp. (April 7, 2006).

[251] Ex Parte of Carroll Wireless et al.

Of course, I support the changes made in this item as DE reform has been an important issue to me for some period of time. In my separate statement to the FNPRM, I talked about a tighter review of DE applications involving large wireless carriers and am pleased that we have extended a thorough Wireless Telecommunications Bureau review to all DE applications. And I applaud the efforts of MMTC in highlighting the need for a more rigorous audit program and advancing proposals that form the basis for those we adopt today. MMTC, like many others in this proceeding, provided thoughtful comments and discussion on the DE program, and has helped create the record that allows us to make at least some changes to the DE program prior to the upcoming AWS auction.

Finally, I must add that I am troubled by the tone and approach of the Second FNPRM. I believe it disproportionally relies on the perceived status of the communications marketplace in assessing changes to the DE program. While I recognize the dual statutory goals highlighted in the item of ensuring opportunities for DEs and preventing unjust enrichment, we also have an obligation to promote competition and innovation in the wireless industry pursuant to Section 309(j)(3)(B), and the DE program is an appropriate vehicle to further that objective. I worry that the Second FNPRM, instead of suggesting proposals that could promote the effectiveness and integrity of DEs, could ultimately lead to determinations that do more harm to potential competition in the communications marketplace than truly protect the program. The item seems to ignore the well-developed record in proposing an unnecessarily complicated and expansive review of perceived problems of the DE program when the solutions already are right in front of us.