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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
)
Implementation of Section 309(j))
of the Communications Act)
Competitive Bidding)

PP Docket No. 93-253

To: The Commission

COMMENTS OF THE TELEPHONE ASSOCIATION OF MICHIGAN

TELEPHONE ASSOCIATION OF MICHIGAN

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SUMMARY

The Telephone Association of Michigan, an association of local exchange carriers in the State of Michigan, supports the Commission's general proposal to provide for certain preferences under the new competitive bidding rules for small businesses, rural telephone companies ("rural telcos") and businesses owned by women and minorities (the "Designated Entities"), especially with respect to broadband personal communications services ("PCS"). However, the Commission's definition of a "rural telco" that would qualify for such preferences is too restrictive and contrary to Congressional intent and should be revised to take into consideration factors such as area served or access lines or eligibility for an REA loan. Additionally, the Telephone Association of Michigan proposes that the Commission allow qualified rural telcos to combine into consortia.

The Commission's proposal to provide for preferential treatment for the Designated Entities is constitutionally permissible and the Commission should provide for channel set-asides and preferential payment terms for rural telcos. Specifically, the Commission should auction broadband PCS spectrum by frequency blocks and should set aside a 20-channel block (Block D) solely for rural telcos. Also, the Commission should use an auction method comprised of sealed combinatorial bids and oral bids for individual markets. Nationwide bidding should not be permitted. Designated Entities should be allowed to pay by installments, and rural telcos should be permitted to use

installment payments for spectrum outside the set-aside block as well as within the set-aside block. Also, rural telcos should not be required to pay an up-front deposit. Rural telcos should also be permitted to apply for PCS spectrum anywhere within the U.S. and not only in the markets where they currently provide service. Finally, there should be a reduced penalty for post-auction disqualification of a rural telco auction winner.

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The Telephone Association of Michigan hereby submits its comments regarding certain proposals set forth in the Notice of Proposed Rule Making, FCC 93-455, released October 12, 1993 (hereinafter "NPRM"), in the above-captioned proceeding.

INTRODUCTION

The Telephone Association of Michigan is an association of thirty-seven (37) local exchange carriers in the State of Michigan. The majority of its members are independent telephone companies.¹ The rest of the Telephone Association of Michigan's members are system companies.² The service territories of all of the members

¹ Allendale Telephone Company, Baraga Telephone Company, Barry Country Telephone Company; Blanchard Telephone Association, Inc.; Bloomingdale Telephone Company; Carr Telephone Company; Chapin Telephone Company; Chippewa County Telephone Company; Climax Telephone Company; Deerfield Farmers' Telephone Company; Drenthe Telephone Company; Hiawatha Telephone Company; Kaleva Telephone Company; Kingsley Telephone Company; Lennon Telephone Company; Ogden Telephone Company; Peninsula Telephone Company; Pigeon Telephone Company; Sand Creek Telephone Company; Springport Telephone Company; Waldron Telephone Company; Westphalia Telephone Company; and Winn Telephone Company.

² Ace Telephone Company of Michigan, Inc.; ALLTEL Michigan, Inc.; Michigan Bell Telephone Company; Century Telephone of Michigan, Inc.; Century Telephone Midwest; GTE North, Incorporated; C,C & S Telco, Inc.; Midway Telephone Company; Ontonagon (continued...)

of the Telephone Association of Michigan other than Michigan Bell and GTE North are essentially rural areas. These comments are being filed by all of the members of the Telephone Association of Michigan except Michigan Bell and GTE North.

The essentially rural nature of these companies is underscored by their sizes in terms of access lines. Excluding the seven largest members of the Telephone Association of Michigan, the largest of the 30 remaining companies provides approximately 6,000 access lines (of which approximately 5,500 are residential lines), and the average of these 30 companies provides approximately 2,100 access lines (of which approximately 1,800 are residential access lines).³ Further, it should be understood that the larger system companies in Michigan were formed over the course of many years by the consolidation of a number of small, rural telephone companies, and that while they serve relatively large areas and have a

²(...continued)

County Telephone Company; Chatham Telephone Company; Communications Corporation of Michigan; Island Telephone Company; Shiawassee Telephone Company; and Wolverine Telephone Company.

³ The 23 independent members of the Telephone Association of Michigan have approximately 44,000 access lines, of which approximately 39,000 are residential access lines, in 46 exchanges, for an average of approximately 1,900 access lines per company (approximately 950 per exchange), and approximately 1,650 residential access lines per company (approximately 800 per exchange). The 12 system companies other than Michigan Bell and GTE North have approximately 159,000 access lines, of which approximately 135,000 are residential access lines, in 117 exchanges for an average of approximately 14,500 access lines per company (approximately 1,350 per exchange) and approximately 11,000 residential access lines per company (approximately 1,150 per exchange). Excluding the five largest of these twelve companies, the average lines per system company drops to 2,800 (750 per exchange) and the average residential lines per system company drops to approximately 2,400 (approximately 625 per exchange).

relatively large number of customers, their service territories are still rural in nature. As potential applicants for the spectrum allocated to the new personal communications services ("PCS"), the members of the Telephone Association of Michigan are acutely interested in the development of the new rules to be promulgated by the Commission for PCS and the competitive bidding process proposed for disbursement of PCS spectrum. The comments herein focus specifically on broadband PCS.

COMMENTS

I. The Commission's Proposed Definition of Rural Telephone Company Is Too Restrictive

The Telephone Association of Michigan supports the Commission's desire to afford certain preferences to small businesses, rural telephone companies, and businesses owned by women and minorities under its new competitive bidding rules. See NPRM, supra, at ¶¶74 & 75. However, the Commission's definition of "rural telephone company" (hereinafter "rural telco") is too restrictive for the purpose of applying any such preferences.

The Commission proposes to define a rural telco as a carrier eligible under §63.58 of the Commission's Rules for exemption from the Commission's telephone company-cable television cross-ownership restrictions (hereinafter "telco/cable cross-ownership restrictions"). See NPRM, supra, at ¶77. Section 63.58 of the Rules exempts from the telco/cable cross-ownership restrictions any telephone company whose proposed service area does not include

- (i) an incorporated place of 2,500 or more inhabitants, or any part thereof; (ii) an unincorporated place of 2,500 or more inhabi-

tants, or any part thereof; or (iii) any other territory, incorporated or unincorporated, included in an urbanized area.

See 47 C.F.R. §63.58(a). The Commission interprets the concept of "service area" under §63.58 to mean not the actual geographic area where the carrier is certificated by the state as the telephone company, but rather the entire community of which the certificated area is deemed to be a part, whether an urbanized area, a municipality or a township, regardless of the fact that the carrier does not provide service to any other portion of the community of which it is deemed to be a part.

The Commission's proposed definition of a rural telco would in effect exclude from the definition and, consequently, from receipt of any preferences, most small, rural and nonprofit telephone companies in this country. This is especially true with respect to rural telcos located within the State of Michigan.

The State of Michigan is divided into three types of municipalities: cities, villages and townships. Even entirely rural areas of the State with no significant population centers are included within townships. Thus, there is no area of the State of Michigan which is not included within some municipality. Typically, the geographical area of the license of a Michigan rural telco will cover portions of one or more municipalities, and rarely conforms to municipal boundaries. In nearly every case, a Michigan telco will be providing basic local exchange service in a part of a municipality whose population exceeds the limitations of the telco/cable cross-ownership rules, although the actual service

territory of the telco will be entirely rural in nature.⁴ In other words, even if the telco is certificated in a rural area with a population of less than 2,500, that rural area is virtually always incorporated into a township with a population over 2,500, making the telco ineligible under the cross-ownership rules. Thus, virtually no telephone company in Michigan can qualify as a rural telco under the definition proposed in the NPRM.

The Commission's proposed definition of rural telco flies in the face of Congressional intent. As noted by the Commission in the NPRM, supra, at ¶72, Congress' objective under subsection (4)(D) of new §309(j) of the Communications Act of 1934 (the "Act")⁵, for directing the Commission to promote the participation of small businesses, rural telcos, women and minorities (the "Designated Entities") in the provision of spectrum-based services was to provide economic opportunities for a larger variety of applicants, including the Designated Entities such as rural telcos. Other Congressional objectives can be gleaned from subsections (3) and (4)(C) of new §309(j), such as the provision of an equitable distribution of licenses to a wider variety of applicants, including the Designated Entities such as rural telcos, and to provide for an expeditious deployment of new technologies, products and services to the public, including those residing in rural areas of

⁴ The Telephone Association of Michigan is aware of only four of its members which are currently providing cable television service through an affiliate under the rural exemption from the telco/cable cross-ownership rules.

⁵ See 47 U.S.C. 309, as amended by §6002(a) of the Omnibus Budget Reconciliation Act of 1993 (the "1993 Budget Act").

the country. Thus, the Congressional intent behind new §309(j) of the Act, in part, is to ensure that as large a variety of applicants as possible, including as many rural telcos as possible, are afforded an opportunity to participate in the provision of spectrum-based services.

The Commission's definition of a rural telco, however, is antithetical to this Congressional intent. Indeed, the purpose behind §63.58 of the Commission's Rules was to foreclose as many telephone companies as possible from qualifying for the exemption from the telco/cable cross-ownership restrictions, thereby ensuring that only those telephone companies serving areas where cable television companies "demonstrably could not exist" would qualify for the exemption. See Telephone Company - Cable Television Cross-Ownership, 50 RR2d 845, 845-46 at ¶¶3-4 (1981). That definition was intended to exclude most rural telcos. Id. Thus, the Commission's proposed definition of rural telco would only serve to reduce the number and variety of participants in the competitive bidding process, in contrast to Congress' intent to expand the number and variety of participants.

A more accurate definition of a "rural telco", and one that advances the Congressional intent behind new §309(j) of the Act, would be one that does not rely solely on the size of the community where the rural telco's certificated area is located, but takes into consideration a variety of criteria that better demonstrate the true nature of the carrier. For example, a carrier's qualification as a rural telco could be based on such factors, in the alternative, as (1) the size of the actual certificated area or

areas served by the carrier, (2) whether the carrier meets the qualifications for a loan from the Rural Electrification Administration, or (3) the number of access lines provided by the carrier.⁶

While such a definition of a rural telco would not be as easily applied by Commission as its own proposed definition, the advantages to the public of a more accurate definition outweigh the administrative disadvantages to the Commission. Indeed, by employing a less restrictive and more accurate definition of rural telcos, the Commission will ensure the participation of such telephone companies in the provision of spectrum-based services and the more expeditious provision of such services to the rural areas of the country. Furthermore, the Commission could put the burden of proof on the carrier to demonstrate its qualifications as a rural telco in its application.

The Commission should also adopt policies which permit qualified rural telcos to combine into consortia, with such consortia eligible to bid for the rural telco setaside spectrum. The Telephone Association of Michigan advocates that a consortium be eligible to bid on rural telco licenses where eligible rural telcos or their 100%-owned affiliates collectively own (both in terms of voting and beneficial ownership) at least 50.01% of the consortium. The Telephone Association of Michigan would oppose a requirement that consortia be composed entirely of rural telcos.

⁶ As to any population-based or access-line-based criteria, the Commission should set the cutoff point substantially higher than 2,500. The Telephone Association of Michigan believes that 10,000 is the lowest figure the Commission should contemplate.

The experience of its members in the cellular arena has been that attracting necessary capital investment to new ventures such as cellular, and now for PCS, may require making equity interests in the venture available to capital providers. That is particularly true with respect to consortia controlled by rural telcos who may be significantly restricted because of the terms of REA borrowings and the requirement of state regulatory approval for any guarantees of financing of their affiliate's non-utility ventures as to the funds they can raise or borrow directly for such a venture. Additionally, in considering appropriate rules to restrict trafficking, the Commission should not preclude transfers among affiliated entities and reorganizations of consortia to permit effective financing and construction, so long as the resulting rural telco licensee still qualifies under the Commission's initial eligibility criteria.

II. The Commission Should Provide For Some Preferential Treatment for Rural Telcos and Other Designated Entities

A. Such Preferential Treatment Is Permissible

The Telephone Association of Michigan concurs with the Commission's general proposal to provide some preferential treatment for rural telcos and the other Designated Entities under the new competitive bidding and PCS rules. See NPRM, supra, at ¶73. In this regard, the Telephone Association of Michigan respectfully submits that the Commission's expressed concerns, NPRM at ¶73, regarding the constitutionality of such preferences are unwarranted. Indeed, Congress has explicitly directed the Commission to promulgate rules providing preferential treatment for

the Designated Entities. See new §309(j)(3)(A), (3)(B) & (4)(C) of the Act.⁷ The Commission is obligated to give effect to Congress' intent and directives. See Metro Broadcasting Inc. v. FCC, 67 RR2d 1353, 1357 (S.Ct., 1990); Beach Communications v. FCC, 70 RR2d 773, 776 (D.C.Cir., 1992). In the case of rural telcos in particular, a preference does not offend constitutional equal protection standards, as rural telcos can be (and are) owned by people of all genders and races.

The Commission's proposals for channel set-asides, tax certificates, and preferential payment terms are rationally related to the legitimate objectives of Congress and are therefore permissible. See Metro Broadcasting, supra, at 1357; Beach Communications, supra, at 780-81. The express objectives of Congress are to promote the participation of rural telcos and the other Designated Entities in the competitive bidding process and ensure an equitable dissemination of licenses among a wide variety of applicants, and to promote economic opportunity for the Designated Entities and competition through the entry of new companies into the telecommunications marketplace. See §309(j)(3)(B), (4)(C) & (12)(D)(4).⁸

Channel set-asides will afford the Designated Entities equal access to the remaining available spectrum, licenses for which they would not be able to acquire through direct bidding competition

⁷ See 47 U.S.C. 309, as amended by §6002(a) of the 1993 Budget Act.

⁸ See 47 U.S.C. 309, as amended by §6002(a) of the 1993 Budget Act.

with larger urban-based entities and their concomitant, advantageous capitalization and access to financing. Additionally, preferential payment terms and tax certificates will provide the Designated Entities with the incentive and the ability to obtain financing which will allow them to participate in the competitive bidding process. Rural telcos, by virtue of their small net worth and income size, face many barriers to the acquisition of financing, including undercapitalization and concentration of ownership, as noted the SBAC's Report. Flexible payment terms and, in appropriate cases, the use of tax certificates will afford greater incentive for financial institutions to provide Designated Entities with the necessary financing to participate in the competitive bidding process. Given the absolutely critical role played by rural telcos in bringing communications services to rural areas, the preference for rural telcos is rational and, therefore, constitutional.

B. The Commission Should Provide For Channel Set-Asides and Preferential Payment Terms For Rural Telcos

The Telephone Association of Michigan agrees with the Commission's proposal to define broadband PCS markets by Basic Trading Areas ("BTA"). Additionally, the Telephone Association of Michigan agrees with the Commission's proposal to auction PCS spectrum by frequency blocks rather than by BTA. Auctioning spectrum by frequency blocks will maximize revenues to the government and will allow applicants to aggregate markets as opposed to aggregating spectrum. The aggregation of markets, unlike the aggregation of spectrum, will ensure the development of viable regional PCS systems.

While the Telephone Association of Michigan agrees generally with the Commission's notion to set aside blocks of spectrum for Designated Entities with respect to broadband PCS, it submits that a separate block of spectrum should be allocated to rural telcos alone. The Telephone Association of Michigan proposes the following set-asides of the 120 MHz of spectrum allotted to broadband PCS:

- 30 MHz (Block A) for all bidders except cellular (MTA licenses)
- 30 MHz (Block B) for all bidders except cellular (MTA licenses)
- 20 MHz (Block C) for minority owned businesses (BTA)
- 20 MHz (Block D) for rural telcos (BTA)
- 10 MHz (Block E) for small businesses and businesses owned by women (BTA)
- 10 MHz (Block F) for all bidders (BTA)

The Commission's proposed auction method of sealed bids for combinatorial bidding for MTAs and oral bids for individual BTA markets is the best approach respecting the D Block set-aside for rural telcos. However, there should be no nationwide bidding for spectrum in the D Block set aside for rural telcos. Nationwide bidding would concentrate all of the available spectrum in the hands of one rural telco, leaving no spectrum for other rural telcos, a result antithetical to Congressional objectives.

The Commission should utilize the following auction method for Block D bids. First, the Commission would accept combinatorial bids for the entire group of Block D (rural telco) licenses within an MTA via sealed bids. Two days later, the Commission would conduct oral auctions for the individual rural telco license in each BTA within that same MTA. Upon conclusion of the oral bidding, the Commission would add up all of the rural telco block

winning bids in each BTA within the MTA and then open the sealed bids and find the winning combinatorial bid. If the winning sealed MTA bid is higher than the aggregate of the individual winning BTA bids, the Commission will award the license to the sealed MTA bid winner. If the sum of the individual BTA bids is higher, then the Commission will award licenses to each of the individual oral auction BTA winners.

The Telephone Association of Michigan also agrees with the Commission's proposal to require a lump sum payment from all bidders with the exception of Designated Entities. Designated Entities should be allowed to use installment payment plans for payment of bids within the set-aside blocks. See NPRM, supra, at ¶¶121. The Telephone Association of Michigan would also support installment payments for rural telcos outside the set-aside blocks. In this regard, rural telcos should not be required to pay any up-front deposit, as proposed by the Commission. The concept of requiring rural telcos to submit large amount of money up-front is inconsistent with the idea of allowing rural telcos to pay a winning bid by installments. Moreover, the excessive financial burden on rural telcos of such a large up-front deposit, given their small size, would only serve to prohibit rural telcos from participating in the spectrum auctions, especially Michigan rural telcos.⁹

⁹ The fact that an up-front deposit poses a financial burden does not call into question the financial qualifications of rural telcos, in light of the relative ease with which a person or entity can obtain financing contingent upon acquiring a license from the Commission. The rural telcos used this method for cellular, without any record of abuse or speculation.

Additionally, a rural telco is already serving the public. Thus, there is no possibility of abuse of the Commission's auction rules or policies. This lack of possible abuse justifies the exemption of rural telcos from the requirement of an up-front deposit. Commission precedent supports disparate treatment of applicants when there is no possibility of abuse. See, e.g., 47 C.F.R. §22.33(b); Rural Cellular Service (Third Report and Order), 4 FCC Rcd 2440 (1988), where the Commission allowed telco cellular applicants to enter into partial settlements for RSAs, even though such settlements were prohibited for non-telcos.

Upon winning a bid, a rural telco should be permitted to pay the bid price through installment payments with interest. To afford the Commission some protection from the risk of default by rural telcos respecting installment payments, each rural telco should be required to provide the Commission with the name, address and telephone number of the financial institution or lender providing the rural telco with the funds used to bid for spectrum. If the rural telco fails to pay an installment, the Commission would then notify the lender of the default and afford the lender an opportunity to cure the default by making the payment due. This will prevent forfeiture of the license, reinstitution of the application/bidding process, and interruption of service to the public. If the lender chooses not to pay the installment due, then the license is immediately forfeit. This procedure will not only benefit the Commission by potentially eliminating the need to conduct new auctions, but will provide lenders with the ability to protect their investments, thereby providing lenders with additional incentive to lend money to rural telcos.

In bidding for PCS spectrum, rural telcos should not be limited to applying for setaside spectrum only in the markets where they are currently providing service. Nothing in the legislative history of the 1993 Budget Act requires such a limitation. The Commission should allow rural telcos to apply for their setaside spectrum anywhere within the United States. The Commission applied this standard for non-cellular Part 22 services,¹⁰ and the result was expedition of conventional mobile telephone and paging services to rural areas. The Commission should follow Bonduel in the PCS arena.

Additionally, rural telcos that have an interest in a cellular license should be permitted to apply for PCS spectrum in the same areas where such telcos hold an interest in a cellular licensee, but other telephone companies and cellular licensees should not be permitted to do so. Because rural telcos are small companies, they will not be able to exercise any kind of market power, in contrast to larger telephone companies and cellular companies which presently do and would in the future exercise such market power.

Finally, while there should be monetary forfeiture imposed on auctions winners whose applications are subsequently disqualified as a means of deterring frivolous or unqualified bidders, the penalty proposed by the Commission (20% of the high bid), see NPRM, supra, at ¶104, is excessive with regard to rural telcos. The Telephone Association of Michigan submits that a

¹⁰ See Bonduel Telephone Co., 68 FCC 2d 497 (1978).

penalty of one percent of the bid price is more than adequate in the ease of rural telcos. There is absolutely no history of abuse by rural telcos, and no real possibility of intentional rule violations occurring. But although there will be no intentional wrongdoing, a sincere, qualified rural telco applicant could ultimately be disqualified for nothing more than a mere oversight in the preparation of its application for which it should not be unduly penalized. The fact that the Commission will retain one percent of a bid price if the auction winner is subsequently disqualified, is enough of an incentive to a rural telco to ensure that there are no oversights or mistakes in its application.

CONCLUSION

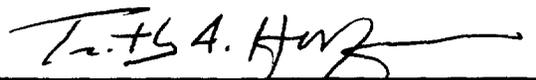
The Commission should define "rural telco" in terms of actual area served or access lines, or eligibility for REA loans, but not in terms of the ultra-narrow cable/telco cross-ownership rules. Rural telcos should get the preference intended by Congress, which preference is rationally related to permissible Congressional goals and therefore constitutional. The Commission should set aside a 20-channel block exclusively for rural telcos. A rural-telco-block bidder should be eligible to bid so long as it is owned at least 50.01% (voting and beneficial) by eligible rural telcos. Combination bidding should be allowed on the rural telco block for MTAs, but not on a nationwide basis.

No deposit should be required from eligible rural telco bidders, and winning bidders should be allowed to pay their bid over time with interest.

Respectfully submitted,

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