DOCKET FILE COPY ORIGINAL

RECEIVED

NOV 3 0 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the matter of	)	
	)	
Implementation of Section 309(j) of the Communications Act, Competitive Bidding	))	PP Docket no. 93-253

Reply Comments of Omnipoint Communications, Inc.

Douglas G. Smith
President

Of Counsel:

Mark J. Tauber
Mark J. O'Connor

Piper & Marbury
1200 19th Street, N.W.
Suite 700
Washington, DC 20036

November 30, 1993

No. of Copies rec'd 0+4
List ABCDE

DOCKET FILE COPY ORIGINAL

RECEIVED
NOV 30 1993
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the matter of:	)	
	)	
Implementation of Section 309(j) of the Communications Act, Competitive Bidding	)	PP Docket no. 93-253

Reply Comments of Omnipoint Communications, Inc.

Omnipoint Communications, Inc. ("Omnipoint") hereby submits its Reply Comments in response to the Commission's Notice of Proposed Rule Making in the above-captioned proceeding (the "NPRM") concerning the implementation of competitive bidding.

Introduction and Summary

As a small business, with great interest in how the FCC conducts the PCS competitive bidding process, Omnipoint offers the following analysis of Comments filed concerning two areas critical to small businesses: the eligibility criteria for small businesses and the sequence of the PCS auctions.

Omnipoint concurs with the majority of comments that addressed the eligibility criteria issue which concluded that the current SBA definition fails to recognize the realities of today's commercial mobile service business and does little to discourage manipulation. Although some comments supported the current SBA definition of a small business, most did so passively and without citing reasons beyond "ease" or "simplicity". In addition, Omnipoint argues that accounting measures such as profits and net worth have too many drawbacks, in that they are difficult to obtain for privately held businesses, are easy to manipulate (even legally), and worst of all, can reward poorly performing larger businesses.

The goal of a small business definition should not be to prevent the creation of new entities specifically for the purpoes of pursuing set-aside licenses, since many if not most, true small businesses will have to create such new entities. Rather, the goal should be to drive capital toward "partnerships" with true small businesses - i.e., "good" shells - and not just fronts for large companies - i.e., "bad" shells.

Omnipoint believes that number of employees and percentage ownership and control by large companies are the best measures for establishing maximum size because these are most directly related to the dynamism (and therefore economic benefits) of small companies.

First, Omnipoint concurs with other comments that 200 employees is a reasonable number because it balances appropriate smallness with sufficient economic scale. Although the number of employees is the best and easiest criteria to administer, it is still subject to abuse and should be safeguarded by two additional tests. First, to prevent larger companies from spinning off subsidiaries and engaging in large scale subcontracting in order to slip under the 200 employee limit, Omnipoint also suggests imposing a revenue limit of $250,000 per employee (or $50 mil total).

Second, Omnipoint concurs with the many concerns raised about large companies setting up "front" or "shell" companies in order to pursue small business preferences. To address this difficult problem, many comments presented useful suggestions to address pieces of the problem. Omnipoint synthesizes below many of these individual suggestions into a framework aimed at protecting true small businesses and consortia, while still allowing large businesses to serve as true minority partners.

As will be detailed below, our recommendation would require 51% voting control by a small business or consortium of small businesses and/or qualified individuals. Any single large company, defined as any company that does not meet any one of the criteria defined herein, would be limited to 49% voting control. Additionally, no more than 70% "equity" ownership (or equivalent if a partnership) of the profits and proceeds can be owned by all large businesses combined. Our proposal also forbids "prior" agreements (i.e., prior to the auctions or the firs three years thereafter) that would provide transfer of ownership or control to a large business at any point in the future. It also forbids very wealthy individuals from unfairly obtaining small business preferences. It imposes a stricter limit on new companies (less than two years old) by forbidding any single large company from owning more than 30% or being the largest shareholder. It provides limited exemptions (i.e., providing higher "equity" ownership but not voting control) to bona fide independent financial companies (such as venture capitalists) to avoid restricting the flow of non-strategic capital and allowing new start-ups to be financed. Lastly, it maintains these limits for the earlier of three years or until the small business licensee meets its first applicable construction requirement (coverage to 50% of pops in the case of PCS).

A second crucial issue to small businesses is the order of the PCS auctions. Omnipoint concurs strongly with the many comments that argue that a "fair start" is critical if the BTA licensees are to have any chance of competing with the MTA licensees and existing wireless services. Having the last pick of antenna sites, distribution/sales channels and OFS relocation options puts smaller companies at an insurmountable competitive disadvantage. Omnipoint concurs with the parties favoring a fair start by auctioning off the BTA licenses within a particular MTA as soon as possible in time to those MTA licenses. To avoid excessive delay to the less populated MTAs, Omnipoint suggests auctioning off only the largest BTAs (and any other BTA with over a certain population) within each MTA before moving on to the next MTA.

I - Eligibility Criteria for Small Businesses

Omnipoint believes the FCC's objective in encouraging the participation of small businesses should be twofold. First, the FCC should ensure that this new industry, and in turn the U.S. economy, fully benefits from the dynamism of true small businesses. As the SBAC Report cited, small businesses create more jobs, operate more efficiently, develop more innovations, and bring innovations to market faster than larger businesses (SBAC Report, p. 5).

Secondly, the FCC should use this opportunity to address some of the inequities that exist in the current telecommunications industry. The existence of monopolies in telephone and cable service has created non-free market incentives that are driving the telecommunications industry towards much higher concentration of ownership. These same forces will be felt in new services such as PCS.

The best way for the FCC to meets its goals for small businesses is to establish eligibility criteria that only allow "true" small businesses to benefit from whatever incentives or preferences the FCC creates (rather than simply an explosion of "bad" shell companies). A "true" small business is one that provides the economic benefits of entrepreneurialism. and mitigates the tendency toward increased concentration of ownership.

Problems with SBA definition

Omnipoint concurs with many of the comments that there is no sound basis for using the existing SBA definition for small business for PCS auction set-asides or preferences. The few parties that supported its use did so mainly on the grounds that it was pre-existing and thereby minimized effort and confusion. Omnipoint would argue that any party bidding on a

PCS license will have to become familiar with so many detailed new issues that understanding a new definition for small business seems insignificant in comparison. More importantly, Omnipoint observed that comments favoring the current definition failed to supply any argument for how or why this definition made sense in the context of PCS or commercial mobile services. In contrast, the parties that argued against using the current SBA definition cited many specific arguments for why it was not a good criteria to be used for the FCC spectrum auctions.

The main arguments against the SBA definition is that it simply does not make sense in the context of PCS and that there are too many ways around the rules. Many comments agreed with the SBAC report which observed that small businesses entering PCS will require much more capital (i.e. net worth) than is typical of other small businesses. (The net worth criteria would also be complicated by the timing of fundraising. Would a small business become ineligible in the middle of the auctions after it had won one license and then raised more money to bid on another?) Comments also agreed with the SBAC's statement that the 1500 employee limit is too high in that it makes many powerful, existing, even dominant telco/cable firms eligible, thereby severely diminishing any advantage intended for true small businesses. Omnipoint also argues, in agreement with Suite 12, that profit-after-tax is a meaningless measure in an industry in which huge players such as TCI and McCaw show little or no profits.

Equally disturbing about the SBA definition as applied to PCS is its over reliance on measures such as net worth and profit-after-tax. For privately held businesses these measures are often closely held secrets for competitive reasons. When these measures are calculated at a specific point in time (as proposed), they can be easily manipulated (even legally) by techniques such as large write-offs or pulling next year's expenses into the current year. Also, these measures are counterproductive in that they accidentally reward poor performance. The FCC's intention of the set-aside is not to accidentally favor large businesses who have lost money for years and as a result reduced its net worth to a level comparable to much smaller companies.

Lastly, Omnipoint concurs with the many comments that expressed concern that the SBA definition's lack of ownership restrictions is an open invitation for large corporations to establish "front" or "shell" companies in order to qualify for the small business preferences.

For these reasons Omnipoint strongly urges the FCC to adopt a new definition for small business that better fits the context of the commercial mobile services industry and ensures that the FCC's laudable goals are met.

An alternative definition

Much research points to, 1) the opportunity for equity ownership by entrepreneurs and, 2) the number of employees as the most important factors that provide small businesses with their exceptional economic dynamism. More than any other measure, a small number of employees with owner/managers is what enables firms to be less bureaucratic and more focused. This in turns leads to more and faster innovation, more efficient operation, and higher growth. Omnipoint therefore proposes number of employees and ownership/voting control to be the main eligibility criteria for small businesses.

Given the operating characteristics of a Commercial Mobile Services business, Omnipoint concurs with the Small Business PCS Association and others that the number of employees should be limited to 200, counted at the time of the auction announcement. A 200 employee limit will include companies that currently have sufficient scale to efficiently initiate a commercial mobile service business. In addition, the 200 employee limit makes sense in terms of getting the economic advantages of small businesses. Once organizations grow much beyond the 200 person mark, they gradually lose the ability to be effectively driven by a small group of leaders and are forced to add layers of management and management processes.

A company's employee count should include all full-time equivalent employees of the company and any subsidiary or affiliate in which the company is the largest shareholder.

Additional safeguards

A) Revenue criteria

Although number of employees is the best indicator of a true small business, even this measure is subject to manipulation. Large scale subcontracting can easily turn a very large business into one with less than 200 employees. However, it is doubtful that a far-flung, loosely knit group of subcontractors would have the same focus, energy and innovative power (on a per person basis) as a true small business. Therefore, Omnipoint recommends that revenues serve as a second criteria for small businesses, since it is less vulnerable to manipulation than other accounting measures. Allowing for highly efficient businesses, Omnipoint believes $250,000 revenue per employee, or a total of $50 million in revenue is an appropriate limit.

B) Ownership criteria

The PCS industry will require large amounts of capital to compete effectively. Thus small businesses will by necessity have to raise capital from either larger businesses, financial institutions, or the general capital markets. Small businesses should be allowed to raise significant amounts of capital from large businesses, but in order to discourage the creation of "bad" shell companies, there should be limits on the ownership of equity and voting control by entities that are not small businesses (as defined herein). These limits should apply for three years from the grant of license, or until the small business meets its first construction requirement, whichever occurs first.

The intent is twofold. First, the rules should encourage larger businesses to invest in true smaller businesses or in new entities controlled by such smaller businesses (i.e. "good shells"). Second, the rules should discourage large businesses from establishing "instant" companies to circumvent the rules (i.e., "bad shells"). The goal is to allow small businesses the flexibility to raise money and compete. The rules should also not prevent the formation of coalitions of small businesses nor should they prevent a truly independent small business from taking on a large business as a non-controlling minority partner. Both types of business relationships will be crucial to the viability of many small businesses.

Omnipoint therefore concurs with many of the comments that small business entities should have a minimum of 51% ownership, defined as <u>voting</u> control, held by individuals, another small business, or group of small business which, on a combined basis, qualify as a small business. (Omnipoint rejects the suggestion put forth by the Minority PCS Coalition (p. 3) that <u>all</u> owners, including minority partners, be counted on a combined basis and made to qualify as a single small business. Omnipoint believes this unnecessarily places too severe a restriction on the fund-raising options of many businesses.) Our proposed definition would limit the interest of <u>any one</u> large company, or its affiliates (defined as any company that does not meet any one of the criteria defined herein) to 49% of voting control. Further, no more than some higher percentage, such as 70%, "equity" control can be owned by all large entities combined. "Equity" control, or its equivalent in other forms such as partnerships, is defined as ownership of the distribution of profits or proceeds.

As a safeguard to prevent a large business from having "de facto" control over a small business, the FCC should forbid "prearranged" (i.e., before the end of the three year period) transfer of ownership agreements between any small business and any large business. In this regard Omnipoint concurs with the comments of Point Communications (p. 3) and others. Specifically, there should be no prior agreement that guarantees the large business, through any mechanism including default, the ability to gain equity or voting control in excess of the stated limits. This is aimed at preventing a large business from setting up a "bad" shell company to bid on and construct a PCS license, while maintaining rights to assume control in the future.

Large companies are likely to respond to whatever eligibility criteria are adopted by inventing creative new corporate structures to circumvent the limits and controls imposed by the FCC. Omnipoint concurs with the comments of Corporate Technology Partners (p. 6) in recognizing this danger, and agree with their definition of a newly formed business as one that is less than two years old at the time of the auction in which it is participating . To discourage such circumvention of FCC rules, Omnipoint suggests a stricter limit on the amount of ownership that large businesses can hold in newly formed small businesses, i.e., less than two years old. Omnipoint proposes that no single large business be allowed to hold more than 30% of equity or voting control of such new businesses. In addition, to prevent a giant from exerting itself over many tiny interest holders, Omnipoint proposes forbidding a large business from being the largest single shareholder (i.e., at least one small business entity must have a larger ownership interest) in these new entities.

One additional criteria the FCC should consider is a limit on the equity and voting control of very high net worth individuals. The prospect of an extremely wealthy individual cashing out of a giant telecomm company and entering the PCS auctions as a preferred small business is somewhat chilling. However, Omnipoint does not want to discourage wealthy individuals from investing in small businesses. Omnipoint proposes an additional criteria for small businesses requiring that no one individual can have more than 49% equity or voting control in a small business, unless that individual is willing to disclose his/her liquid assets which must be less than $X million. However, if the individual puts up less than $Y million of his/her personal capital to obtain the 49% level, then the company would still qualify as a small business, and the individual would be exempt from disclosing his/her net worth.

The combination of the above criteria work together to protect true small businessesm and encourage investment in existing small businesses. Importantly, they also allow for the formation of consortia of true small businesses while still allowing large businesses to serve as true minority partners.

The one exception to the "equity" control restriction stated above would be to allow independent financial services entities (i.e., not controlled by, or affiliated through strategic relationships with, a large corporation with ongoing non-financial businesses) to hold up to 70% equity but still not more than 49% voting control of common stock (or conversion into common stock). This exception avoids creating barriers to raising funds in the capital markets. More importantly, it allows true entrepreneurial start-ups to raise significant capital, but prevents large corporations from creating "bad" shell companies.

C) Transferability to large business

If a small business has a license which was set aside exclusively for small businesses, then that small business should be required to meet its first FCC imposed construction deadline, or wait 3 years after issuance of license, whichever occurs first, before transferring the license to a large businesses. A license can be transferred to another qualified small business entity at any time.

All other licenses should be freely transferable.

II - Structure of Auctions

A) Sequence of Auctioning Spectrum Blocks and Service Areas

The NPRM proposes to auction PCS licenses by first auctioning off all Block A licenses in the 51 MTAs, then moving to Block B, then Block C, etc.. Omnipoint opposes this as unfair to small businesses as do many other commenters that strongly advise against such an approach.

The NPRM states that the broadband PCS auctions will be used to conduct a "significant test" of group or combinatorial bidding at the national level. However, it is unclear why the FCC is creating this national exception when only three companies out of 147 commenters in the PCS docket supported national licenses. The creation of a nationwide PCS license is neither a goal of Congress nor the FCC. In fact the FCC explicitly decided not to allocate national licenses for broadband PCS. In the first round of comments on this NPRM, all but a handful of the commenting parties resoundingly rejected the goal of increasing the likelihood of a nationwide PCS license. With oral bidding there is an obvious way to aggregate licenses to national coverage.

The unfortunate by-product of the NPRM's proposed plan is that now the "starting point" for the PCS auction design is the proposed, "auction off all Block A licenses first". It is unfortunate because of the extreme inequity that this plan creates for the small businesses that will be bidding on the 20 MHz and 10 MHz licenses. These small businesses will have a hard enough time competing with the 30 MHz licensees and the entrenched cellular providers. It is imperative that the FCC at least allow the small businesses to start the race at the same time as their bigger competitors.

The 20 MHz and 10 MHz licensees, already disadvantaged by their smaller allocation, require an "even start" with the larger 30 MHz licensees to ensure the following:

1) An early start on relocating OFS users. (Note that nationwide, on average, each 10 MHz licensee will have to relocate a 24% higher number of OFS links than each 30 MHz licensee will have to relocate) The PCS licensees that start relocating OFS links first will have a much better selection of available options for relocation.
2) Access to the very few good antenna sites that are still available in urban areas.
3) Access to the best sales and distribution channels. (Many large retail chains have already signed exclusive agreements with cellular companies.)

Perhaps most importantly, allocating the 2100 MHz licenses early also helps jump start the market for 2100 MHz equipment (currently non-existent) by creating real, paying customers as soon as possible. All of these above factors will be critical to the success of any PCS player, but absolutely vital to the smaller players who have less ability to "buy their way out" of any setbacks they encounter.

If the FCC were to pursue its proposed course of auctioning off each frequency block one at a time (going through all 51 MTAs for block A before moving on to block B) the results could be devastating for small businesses. Especially hard hit would be those that can only afford the 10 MHz BTAs. These would be auctioned off after the "Big PCS" licensees were well on their way. It is likely that such a competitive disadvantage against an entire class of participants would worsen the prospects of small businesses raising the money necessary to bid on and construct PCS licenses.

A Better Auction Design

Given that BTA licensees will be in competition with MTA licensees, Omnipoint submits that any auction design that gives one entire class of participants - large entities - a significant head start over the other is unfair. At the same time, Omnipoint realizes that the process of sequentially auctioning off every BTA license within an MTA before moving onto the next MTA will also slow the licensing of many major cities in the U.S.. Business and consumers interested in the early deployment of PCS in the big cities of the smaller MTAs would be unfairly delayed. For example, Kansas City, the 24th most populated BTA, would have to wait for 2004 other auctions to be completed.

<u>As a compromise between the two extremes of sequential auctions Omnipoint offers an alternative</u>. The FCC should start with the MTAs in descending order. First, auction off the MTA licenses in each MTA area. Then, for a limited number of the largest BTAs within that MTA, auction off all 5 frequency blocks for each designated BTA. Then move onto the next MTA region. This approach balances the desire to quickly progress through all of the MTAs while allowing the larger BTA licensees to get an "even start" in those markets where the MTA licensee will most likely deploy first.

For example, the top BTA and any BTA with over 1,000,000 population within the MTA could be auctioned off in this first round.

This balanced approach to the auction sequence has other benefits. It will allow faster aggregation of the smaller BTA spectrum blocks into larger, more viable ones. The FCC specifically stated in its PCS Report & Order that aggregation of the 20 MHz and 10 MHz licenses into larger blocks is an expected and even desirable outcome. Indeed, at least two of the 10 MHz licenses would probably have never been allocated had it not been for the prospect of aggregation into larger blocks. It is clear from the record that the easy and fast aggregation of small spectrum blocks into larger ones is, at a minimum, at least as important as the aggregation of MTA licenses into regional or national blocks.

Finally, the FCC should weigh carefully the arguments of parties favoring the "all block A first" approach. In reality, the alternative proposed above will not impose any significant delay on the deployment of a nationwide system, if one were to be won. Considering the enormous amount of capital involved, any nationwide system will be rolled out over time, probably from most densely populated region to least. Slightly delaying the auction of the less populated MTAs may delay the ability of a national bidder to say; "I've won a nationwide license", but it will not delay that company's deployment plan. Deployment of service is what matters to the public.

B) Simultaneous Auctions

While "simultaneous" auctions solve some problems and have a certain theoretical appeal, Omnipoint believes simultaneous auctions will be problematic for small businesses and the FCC. Omnipoint discourages the Commission from adopting them for PCS for the following reasons.

For such a system to work, each company that wants to bid will almost certainly have to be equipped with a computer system connected to some central auction computer. The additional cost and learning curve associated with that system will disadvantage a small company. In addition, the analysis required to correctly analyze many simultaneous, interrelated auctions is immense. The problem is made even worse if the FCC allows all possible geographic combination of bids. Omnipoint believes that a large company, with its teams of analysts, programmers and high speed computers will have a significant advantage over a smaller player trying to buy even a single BTA, let alone piecing together a number of small BTAs in order to compete effectively with larger regional players.

The disadvantages to the FCC are twofold. First is the increased burden of developing, implementing, deploying, and training users on what will inevitably be viewed as a complex system. Omnipoint questions whether it is possible within the Congressional deadlines to develop, debug, document, train, and allow testing of such simultaneous systems. Second is the loss of the ability to fine tune the auction system as the auctions progress. In a sequential auction scheme, any problems discovered in the first few auctions can be corrected in later rounds. With one big simultaneous auction, the whole process is over before you have any idea of how well it worked or whether any unintended flaws or outcomes resulted. Thus, simultaneity is a risky approach for an agency that has never before administered auctions.

Douglas G. Smith
Douglas G. Smith
President