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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	)	
	)	
Inquiry on Competitive Bidding	)	
Process for Report to Congress	)	Docket No. WT 97-150
	)	

To: The Commission

COMMENTS OF IRIDIUM LLC

Iridium LLC ("Iridium"), by its undersigned counsel, hereby responds to the Commission's Public Notice, FCC 97-232, released July 2, 1997, in which the Commission requested comments concerning the competitive bidding process for spectrum, in anticipation of the Commission's report to Congress as required by Section 309(j)(12) of the Communications Act of 1934, as amended.

Iridium is on record with the Commission in IB Docket No. 96-220[1/] and other proceedings opposing the use of competitive bidding (auctions) to select licensees from among mutually exclusive Mobile Satellite Service (MSS) applicants.[2/] As Iridium pointed out in that proceeding, auctioning spectrum for MSS licenses will not hasten the development or deployment of new services because of the global nature of MSS service. Using an auction in that context would do nothing more than confer upon the

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1/ Amendment of Part 25 of the Rules Pertaining to Second Processing Round of NVNG-MSS Systems, IB Docket No. 96-220.

2/ Comments of Iridium LLC in IB Docket No. 96-220, filed December 20, 1996, at 5-9.

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successful bidder a license to operate in the U.S. -- a license that is only one of approximately 200 licenses needed to operate a global system. If anything, use of auctions by the U.S. would actually impede deployment of global service because of the likelihood that other nations would follow suit, resulting in a series of sequential auctions in numerous different countries that would create uncertainty for potential service providers, a problem that was recognized by the Commission itself in its Notice of Proposed Rulemaking in IB Docket No. 96-220.[3/] This and other problems that would result from using auctions for global MSS spectrum were described in detail in the study entitled "Public Harms Unique to Satellite Spectrum Auctions" by Strategic Policy Research, March 18, 1996, transmitted to the Chief of the Commission's International Bureau on March 21, 1996,[4/] a copy of which is being filed today in this proceeding by the Satellite Industry Association (SIA). Iridium endorses the findings and conclusions of that study, as well as the comments filed today in this proceeding by SIA.

Not only has the FCC itself recognized that using auctions for global satellite services would present a number of complex issues, but the U.S. Congress has recognized this, as well. In the Conference Report pertaining to Title III of HR-2015, the Balanced Budget Act of 1997 passed by the House and Senate this week, the

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3/ NPRM in Docket No. 96-220 released October 28, 1996, at paras. 80-81.

4/ Letter to Scott Blake Harris from Satellite Industry Association, dated March 21, 1996.

Conferees observed that the statutory revisions to the language in Section 309(j) of the Communications Act "should not be construed as a Congressional endorsement of auctions for licenses to offer global satellite services," noting specifically that "the treatment of global satellite systems raises numerous public policy questions beyond the issue of spectrum auctions."[5/] The Conferees also pointed out that, notwithstanding the expansion of auction authority contained in the 1997 Budget Act, the FCC must still ensure that its determinations regarding mutual exclusivity -- a statutory condition precedent to the use of the Commission's auction authority -- are consistent with the obligations under Section 309(j)(6)(E) of the Act. In this regard, the Conferees stated that they were particularly concerned that "the Commission might interpret its expanded competitive bidding authority in a manner that minimizes its obligations under Section 309(j)(6)(E), thus overlooking engineering solutions, negotiations, or other tools that avoid mutual exclusivity."[6/] Lest the Commission adopt such an interpretation, the Conferees admonished the Commission that spectrum auctions were not to be used for all licensing under all circumstances. Iridium agrees with that approach, and respectfully urges the Commission that auctions not be employed for the licensing of global MSS systems.

As noted at the outset, Iridium's interest in this matter is limited primarily to the use of auctions for awarding licenses for global MSS systems. Notwithstanding the

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5/ Congressional Record, July 29, 1997 at H6173.

6/ Id.

limited scope of its interest, Iridium nevertheless wishes to comment on several questions posed by the Commission in its July 2 Public Notice. First, the Commission requested comment on how competitive bidding has facilitated the introduction of new technologies and the entry of new companies into the telecommunications market.[7/] In response, Iridium notes that there does not appear to be a direct, positive correlation between use of auctions and the rapid introduction of new technologies by new companies. Although the A Block and B Block PCS auctions were followed closely by the introduction of new technologies and services in the marketplace, several other auctions conducted by the Commission have not produced tangible results in the form of new services. Notably, the auction for Interactive Video Data Service (IVDS) licenses, one of the first auctions to be held (in mid-1994), has yet to result in the introduction of <u>any</u> new service in that band in <u>any</u> location. It would appear that the rapid introduction of new technologies and new services has more to do with the availability of equipment and capital than with the auction process itself.

The Commission also requested comment on how the competitive bidding rules have insured that small business, rural telephone companies and businesses owned by women and minorities have been able to participate successfully in the competitive bidding process. A good and timely answer to that question may be found on the

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7/ July 2 <u>Public Notice</u> at 5.

front page of the August 1, 1997 issue of The Wall Street Journal[8/] reporting on the results of the C Block auction, which was designed to place PCS licenses in the hands of small businesses. According to the press account, the C block auction has become "a $10 billion fiasco" characterized by defaults by the winning bidders, bankruptcies and threats of bankruptcies. It remains to be seen whether any of the C Block auction winners ever will actually commence provision of wireless communication services to the public. Suffice it to say for the moment, however, that the auction process, in and of itself, does not appear to have conferred upon all of its intended beneficiaries the advantages that were anticipated by many, including the Commission.

In its July 2 Public Notice, the Commission also stated that as a result of auctions "the public is now receiving the direct financial benefit from the award of licenses."[9/] While it is true that "the public" has benefited recently from the government's collection of significant spectrum auction revenues, it is not clear that "the public" will be the permanent beneficiary of those collections. Instead, it is more likely that "the public," in its role as consumers, will be required to pay back those revenues eventually. Sound business practice dictates that, in the long run, the spectrum acquisition costs incurred by the auction winners be passed on to

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8/ See attached copy of The Wall Street Journal article entitled "FCC Auction Designed to Favor Little Guys Threatens to Sink Some."

9/ July 2 Public Notice at 4.

subscribers, and it is "the public" who will constitute the subscriber base that must make those payments. In other words, what goes into one "public" pocket in the form of auction revenues inevitably will come out of another pocket in the form of increased prices for services. The result will be a wash, which means in essence that there will not be any true recovery for "the public" of the value of the spectrum in the long run.

Iridium urges the Commission to include in its report to Congress an assessment of the shortcomings and limitations of the auction process, as well as its benefits. As a related matter, we also suggest that it is essential for the Commission to portray to representatives of other nations the total picture concerning spectrum auctions in the U.S. Historically, the U.S. has been the world leader in developing and using telecommunications technology, and this leadership position is in no small measure linked to our regulatory framework governing telecommunications. The rest of the world looks to the U.S. and often emulates it in this field, as witnessed by the worldwide impetus in recent years toward privatization and deregulation in the telecommunications sector. Given the limited experience with auctions thus far and the mixed results they have achieved, it is important for the U.S. to communicate clearly to the rest of the world: (1) that the experiment with auctions in the U.S. has been just that -- an experiment; (2) that the scope of the experiment has been limited to domestic-only wireless services; (3) that the results of the experiment have thus far been mixed; and (4) that spectrum auctions are not a "one-size-fits-all" solution to every spectrum management problem. Specifically, Iridium recommends that the

Commission adopt a policy of requiring its spokespersons -- in speeches and other presentations at multilateral and bilateral meetings with representatives of other nations -- to make absolutely clear that spectrum auctions are not an appropriate licensing mechanism for all types of wireless services, particularly global MSS systems.

In conclusion, Iridium respectfully requests that the Commission include in its report to Congress an acknowledgment that use of competitive bidding for awarding licenses for global MSS systems is not an appropriate exercise of the Commission's auction authority.

Respectfully submitted,

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August 1, 1997

Best of Intentions

FCC Auction Designed To Favor Little Guys Threatens to Sink Some

Payment Terms for Licenses Were Easy, So Firms Bid Billions They Didn't Have

Looking for the Cheap 'Pops'

By QUENTIN HARDY
And BRYAN GRULEY
Staff Reporters of THE WALL STREET JOURNAL

One year ago, the Federal Communications Commission pulled off what looked like a dazzling two-fer. Aiming to help entrepreneurs compete with entrenched giants, the FCC auctioned off hundreds of new licenses to provide wireless telephone, paging and other services. The auction fetched a stunning $10.2 billion, and FCC Chairman Reed Hundt boasted about the "courage" of "these steadfast entrepreneurial winners . . . to compete in the wireless marketplace."

No one is bragging now. A slew of bidders, blaming a deteriorating market for wireless stocks, say they can't pay for their licenses, and they are threatening to file for bankruptcy if the FCC doesn't bail them out. The government could collect billions of dollars less than was promised. And the licenses that were supposed to foster competition could instead languish in court for years.

"It's unfortunate that we've been put in this position, but here we are," says Mr. Hundt, the regulator who has been thrust into the unfamiliar role of banker.

Having failed to persuade the Treasury Department to take over debt collection, Mr. Hundt has been forced to hire outside bankruptcy lawyers while the agency's own communications lawyers bone up on bankruptcy law. He and his fellow commissioners have spent the past month listening to pleas from troubled bidders who want the FCC to cut their debt or ease their payment terms.

Meantime, Wall Street is demanding a quick solution while other bidders and aggrieved rivals are threatening to sue if the FCC capitulates. Congress is watching as it considers whether to limit future auctions of rights to use the electromagnetic spectrum. And a big embarrassment looms for the Clinton administration, which has touted auctions as a crowning achievement of its telecommunications policy.

Attractive Terms

Why the "C-block" auction has become a $10 billion fiasco is a tale of seemingly good intentions gone awry. Seeking to help little players enter the telecommunications game, the FCC offered an installment-payment plan that would help them buy licenses. Instead, the attractive terms artificially inflated the bidding and scared off Wall Street, which decided some bidders had paid way too much to be the fifth or sixth wireless competitors in the market.

The C-block auction is a bit of an anomaly, albeit a potentially costly one. In 14 spectrum auctions in three years, the FCC has collected nearly $12 billion, including $1 billion so far from the C-block auction. The auctions have put 4,377 licenses in the hands of companies vying to offer phone, paging, radio and other services—and Mr. Hundt says fostering competition remains his priority as he determines what to do about the troubled C-block bidders.

Last year, he shrugged off suggestions that some bidders had overpaid, saying he was "indifferent" to the prices and insisting deadbeats would have licenses taken away for reauction. He defends negotiating with bidders now as a logical reaction to the threat of bankruptcy litigation. "Bankruptcy is not swift, it's not smooth, it's not certain," he says. "It's a fundamental problem because I don't want the licenses on ice."

But it is increasingly doubtful that big bidders are going to get much, if any, relief. "I've met with quite a number of players and no one has made a compelling case for significant modification," says FCC Commissioner Susan Ness, who used to handle loans to communications companies as a banker. She thinks the FCC might make minor changes, but says, "mainly, you make your payments or you lose your licenses." Commissioner Rachelle Chong has expressed similar thoughts, and even Mr. Hundt vows a "tough minded" approach with the largest bidders: "They have a lot of sunk costs and a lot of assets to protect and we think they have a lot of incentives to pay."

Winning Bids

In 1993 Congress authorized the FCC to auction communications-spectrum licenses. The FCC made a splash by raising $7.7 billion with its auction of the so-called A- and B-blocks in 1995. Giant companies such as AT&T Corp. paid for winning bids with cash up front.

The C-block auction was designed, at Congress's behest, to distribute licenses to small businesses, rural phone companies and businesses owned by minorities and women. In addition, Congress urged the FCC to offer helpful financing such as installment payments.

A landmark 1995 Supreme Court decision scuttled special treatment of women and minorities, so the FCC designed the C-block to help small companies with annual revenues of less than $40 million. Bidders were allowed to pay over 10 years at below-market rates, with interest-only payments for the first six years.

Experts now say the terms were a

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FCC Auction

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crucial flaw. "An initial six years of interest-only payments increases the likelihood of speculation," says Peter Cramton, a University of Maryland economics professor who helped design the structure of an earlier auction. "If anything, you'd want a higher up-front payment from a new company, to reduce the risk of default."

The C-block auction began in December 1995 with 255 bidders and ended with a reauction of some properties in July 1996. Many of the "entrepreneurs" weren't small fry, though.

Top executives of NextWave Telecom Inc. of San Diego include former FCC adviser Janice Obuchowski and Allen Salmasi, once president of wireless operations at Qualcomm Inc., a big maker of digital-communications gear. Qualcomm, Sony Corp. and South Korea's Pohang Iron & Steel Co. all pledged bidding money to NextWave, which topped all bidders by offering $4.2 billion for 63 licenses. Pocket Communications Inc., of Washington, D.C., which bid $1.4 billion, was started by Daniel Riker, a former senior executive of MCI Communications Corp., and had backing from Westinghouse Electric Corp. and a consortium of Asian investors.

Though well-connected, many companies started with nothing like the money needed to pay for their spectrum in full. Typically, there was enough for a modest down payment, and a plan to use the spectrum to raise more money. Pocket entered the auction with "something like $80 million" in capital and eventually raised about $180 million, Mr. Riker says.

For most bidders, getting spectrum was crucial to their survival. "With no license, there's no business, but there just isn't room for that many small companies," says Prof. Cramton. (He advised Pocket during the auction, but declines to discuss his work for the company.)

Many bidders targeted certain cities, putting further upward pressure on bidding in those areas. Pocket, which hoped to unite digital cellular networks on the East and West Coasts, bid heavily for licenses in Chicago and the Midwest. Omnipoint Corp., Bethesda, Md., which had earlier picked up properties in the New York area, went after Philadelphia. NextWave, which has an unorthodox plan to resell its services using commercial providers like MCI, also needed national coverage for its plan to work.

Executives also projected high sales, and drew hope from a hot stock market. Omnipoint, which already owned some wireless licenses, saw its January 1996 initial public offering at $16 a share soar 75% in one month. The stocks kept climbing with the size of the C-block bidding, almost as if the two fed on each other.

The result was "a brawl," says Pocket's Mr. Riker. For many, bidding rapidly escalated beyond the levels of the A- and B-block auctions. Those bidders had paid an average of $15.54 per "pop," an industry term for a potential customer. C-block participants wound up bidding an average of $39.88 per "pop." But most of the problem was with the top 10 bidders, who offered about $8 billion. Most of the other bidders actually bid close to or less than comparable A- and B-block levels, FCC officials say.

'Exquisitely Painful'

Even larger outfits such as NextWave were daunted by the number and size of the bidders. "It was fiercely competitive, beyond people's control," says Mr. Salmasi, NextWave's president. "We had to bid prices into the mid-$30s a pop" just to thin out the competition.

"It was exquisitely painful," says Steve Hillard, a representative of the Cook Inlet Alaskan Native Corp. of Anchorage, a minority-owned company seeking wireless properties in the West and Southeast. "We hoped for $7 a pop, and we were ready for up to about $20.

"The bids went past that within a few weeks. We were heartbroken. We'd spent a year and a half helping to write the legislation, finding the best partners we could, then seeing a prudent business plan get curtailed by speculation. Every night, we'd talk about another opportunity that had been ruined." The Alaskans pulled out of their partnership with BellSouth Corp., but won the bidding on a few cheaper properties, such as Tulsa, Okla., and Spokane, Wash.

Some big players with plenty of industry experience pulled out as the bidding got too high. Among these was Craig McCaw, the wireless-industry pioneer who sold his company to AT&T for $11.5 billion in 1994 and who was trying to set up a new venture. Mr.McCaw says the bidding spelled doom for many.

If the FCC was aware of its mounting problem, nobody inside the agency admitted it. At an investment conference in March 1996, Michele Farquhar, then chief of the FCC's Wireless Bureau, said, "We will not stop the bidding because spectrum is supposedly overpriced."

At a wireless convention in Dallas, Kevin Compton, a partner at the Palo Alto, Calif., venture-capital firm of Kleiner Perkins Caufield & Byers, says he warned Mr. Hundt: "Within one year, you'll have to change your . . . rules and payment schedules. If you don't, all the lawyers who have been trying to understand your crazy FCC bidding rules will be trying to understand bankruptcy laws."

No way, Mr. Hundt replied. He was equally emphatic in warning conference attendees that the FCC wouldn't accept defaults. "Forget about it," he said in a speech. "We have long had plans to reauction defaulted licenses right away."

Watching gleefully from the sidelines were the big companies that the FCC had hoped to threaten with a horde of new rivals. "We were passing around internal memos that showed how much more they paid for their properties than we did," says Wayne Perry, formerly vice chairman of AT&T's wireless division, and now president of Mr. McCaw's OneComm Corp.

Excess Competition

Meantime, challenges from disgruntled bidders delayed FCC issuance of licenses to NextWave, Pocket and others. By September, some were hinting they might have trouble paying. In a letter to the FCC, NextWave's Ms. Obuchowski told her former colleagues they "must recognize the fundamental difficulties companies face in gaining access to capital," and recommended that her company receive a one-year deferral of interest payments.

By the time NextWave and others started getting their licenses, Wall Street was souring on wireless start-ups. Beset by technical glitches, problems putting up antenna towers and fears of excessive competition, the sector was trashed. Omnipoint's stock, which had peaked at $35.50 a share in October, crashed to $6.63 this April. It currently trades at $15.3125 a share. Just as the bidders had justified high bids with high market valuations, the crash now reduced their chances for obtaining financing.

NextWave has filed for both an initial public offering and public debt, but has withheld both for fears they would fail. Mr. Salmasi says investors don't accept his projections about the size of the market, and in a cautious turn, have demanded to see real earnings, rather than cash-flow projections. "There was a change in market psychology," he says.

Pocket's Mr. Riker saw bankers' doors close as he tried to assemble an initial public offering to pay for equipment, staff and auction payments. "Just after the auction, we had talked to Bear Stearns, Goldman Sachs and Cowen & Co. They were all hot to go," says Mr. Riker, who eventually teamed with Donaldson, Lufkin & Jenrette Inc. "Then Omnipoint [stock] crashed, and the prices at the next auctions were down 80%. The bankers started explaining the facts of life to us."

On April 1, Pocket filed for Chapter 11 bankruptcy protection after it couldn't find $1.8 million for an interest payment to a backer. Just the day before, the FCC had stopped taking all interest payments from the bidders, saying it wanted to consider letting them make payments annually rather than quarterly. Pocket, NextWave and other troubled bidders stepped up their calls for relief, and soon the FCC confronted a raft of proposals to restructure bidder debt, including reducing it by more than half and eliminating interest payments for eight years. Mr. Hundt toned down his tough talk about reclaiming licenses because companies were threatening to shield them in bankruptcy — a danger the FCC was aware of last year but didn't consider a significant threat.

FCC lawyers say that while a 1934 communications law says licenses aren't considered part of a bankruptcy estate, some courts, relying on the Bankruptcy Code, have ruled otherwise. Without a clearer legal picture, FCC officials fear licenses in bankruptcy could be tied up in court for several years, an eternity in the telecommunications business.

The FCC has been asking Congress to clear up the uncertainty, and Mr. Hundt says he hopes to persuade lawmakers to act by the end of September "so we can dictate the terms of surrender instead of being mired in the bankruptcy swamp."

Now the FCC finds itself in a multibillion-dollar game of chicken with NextWave, Pocket and other big bidders. An FCC task force headed by staffer Jon Garcia, a former McKinsey & Co. consultant, is working to devise a solution that will win the support of at least three of the four FCC commissioners.

While Mr. Hundt has hinted he especially wants to help small, rural competitors, other commissioners have argued that any changes would encourage bidders in future auctions to bid irresponsibly in the belief that the FCC will ease their obligations. Ms. Ness says any significant step also would be unfair to bidders that withdrew from the C-block auction, competing bidders and companies that won licenses in other auctions. "It seems to me the marketplace should be allowed do its will," she says. But the commission is seriously considering small steps, such as an amnesty program in which bidders would be forgiven debts and penalties if they return licenses for reauction.

The primary goal, Mr. Hundt says, is to get licenses to companies that will build phone systems and start competing. "This is not a bad policy, but people in Washington have to realize if you're going to follow this policy, you're going to have to act like people on Wall Street," he says. "It would be easy to do nothing, but that's not commercially reasonable, that's not what lenders do, and that's not good communi-

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 1st day of August, 1997, caused copies of the foregoing "Comments" to be served by first class mail, postage prepaid to the following:

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