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## I. INTRODUCTION

1. In this *Sixth Memorandum Opinion and Order and Further Notice of Proposed Rule Making*, we resolve petitions for reconsideration<sup>1</sup> of our rules governing the methodology and procedure for auctions to provide interactive video and data service (IVDS), and propose modifications to our competitive bidding rules for the upcoming auction of IVDS licenses.<sup>2</sup> Specifically, we reexamine various aspects of the *Fourth Report and Order* concerning: (1) the establishment of our July 28-29 IVDS auction dates prior to a determination that mutual exclusivity existed; (2) the prohibition of settlement among mutually exclusive applicants; (3) modifications to our upfront and down payment provisions; and (4) provisions established for

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<sup>1</sup> Petitions for Reconsideration were filed by ITV, Inc. (ITV), Phase One Communications, Inc. (Phase One), the Rural Cellular Association (RCA), and U.S. Intelco Networks, Inc. (USIN). Oppositions/Comments were timely filed by Quentin L. Breen (Breen) and the U.S. Telephone Association (USTA). In addition, the Interactive Television Association (ITA) filed a petition for rule making.

<sup>2</sup> IVDS is a point-to-multipoint, multipoint-to-point, short distance communications service. IVDS licensees may provide information, products, or services to individual subscribers located at fixed locations within a service area, and subscribers may provide responses. Examples of service offerings that licensees could offer include opportunities for real-time responses to polls, educational or pay-per-view programming, and commercial data applications, such as transmission of database information to point-of-sale terminals, home banking or downloading of data to personal computers, VCRs, or other consumer electronic products. See Amendment of Parts 0, 1, 2, and 95 of the Commission's Rules to Provide Interactive Video and Data Services, *Report and Order*, GN Docket No. 91-2, 7 FCC Rcd 1630 (1992).

designated entities. We also make certain modifications on our own motion pertaining to our auction methodology. In addition, we propose certain changes in our designated entity rules in order to address legal requirements of the Supreme Court's decision in *Adarand Constructors, Inc. v. Peña (Adarand)*.<sup>3</sup> In proposing these modifications, we reiterate the Commission's statutory obligation to ensure that small businesses, businesses owned by women and minorities, and rural telephone companies (collectively, "designated entities") are afforded opportunities to participate in the provision of spectrum-based services.<sup>4</sup> We remain committed to this goal. We also propose to increase the upfront payment amounts for bidding on IVDS licenses.

## II. EXECUTIVE SUMMARY

2. This Executive Summary summarizes the principal decisions and proposals made regarding competitive bidding rules for IVDS in this *Sixth Memorandum Opinion and Order and Further Notice of Proposed Rule Making*

### A. Sixth Memorandum Opinion and Order

- Denies petition asserting that the Commission must determine that mutual exclusivity exists before establishing auction dates or publicizing auctions.
- Denies petition to permit applicants to communicate with one another following the short-form application deadline.
- Amends rules to enable the Commission to conduct future IVDS auctions using simultaneous multiple round bidding.
- Grants petition so that the Commission will refund upfront payment amounts to the extent that they exceed the required down payment.
- Denies petition to reduce the amount of the default payment from the smaller of three percent of the subsequent winning bid (or three percent of its own bid) to zero, if the subsequent winning bid exceeds the defaulting applicant's bid by three percent or more, otherwise the difference between the subsequent winning bid and 103 percent of the defaulting applicant's bid.
- Grants petition to make bidding credits available to both licenses in each IVDS service area.

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<sup>3</sup> \_\_\_ U.S. \_\_\_, 115 S.Ct. 2097, 132 L.Ed. 158 (1995).

<sup>4</sup> Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, Title VI, § 6002(a), 107 Stat. 312, 388 (1993) (Budget Act).

- Eliminates the tax certificate program available to investors in women- and minority-owned businesses in accordance with Congressional action.
- Denies petition to not apply unjust enrichment provision for the transfer of a license obtained using bidding credits when the license is assigned or transferred at a loss, and to base the payment on a profitable transfer on the profits attributable to the license, and not the government's cost in providing the bidding credit.
- Denies petition to grant rural telephone companies special provisions beyond what they are eligible for under the other designated entity provisions.

**B. Further Notice of Proposed Rule Making**

- Tentatively concludes that the race-based provisions in our competitive bidding rules for the IVDS auction are not presently supported by a record that can withstand the strict scrutiny standard of judicial review required by the Supreme Court's ruling in *Adarand*, and seeks additional evidence to support these provisions.
- Tentatively concludes that the gender-based provisions in our competitive bidding rules are not supported by an adequate record, and seeks additional evidence to support these provisions.
- In the absence of sufficient supporting data, proposes to make our IVDS rules race- and gender-neutral.
- Seeks comment on whether our definition of small business continues to be appropriate.
- Seeks comment on whether and how we should extend bidding credits to small businesses.
- Tentatively concludes to increase the upfront payments from \$2,500 for every five licenses won to \$9,000 per Metropolitan Statistical Area (MSA) license won, and \$2,500 per Rural Statistical Area (RSA) license won.

**III. BACKGROUND**

3. In the Omnibus Budget Reconciliation Act of 1993 (Budget Act), Congress authorized the Commission to award licenses for certain spectrum-based services by competitive bidding.<sup>5</sup> In authorizing the use of auctions, Congress directed the Commission to "ensure that small

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<sup>5</sup> Budget Act, Pub. L. 103-66, Title VI, § 6002, 107 Stat. 312, 388.

businesses, rural telephone companies, and businesses owned by members of minority groups and women [collectively known as 'designated entities'] are given the opportunity to participate in the provision of spectrum-based services."<sup>6</sup> In the *Second Report and Order* in this proceeding, the Commission exercised its authority by determining that IVDS licenses should be awarded through competitive bidding and by prescribing general rules and procedures and a broad menu of competitive bidding methods to be used for all auctionable services.<sup>7</sup> We reexamined certain aspects of these general rules and procedures in the *Second Memorandum Opinion and Order*<sup>8</sup>

4. In the *Fourth Report and Order* in this docket, we established specific competitive bidding procedures for IVDS.<sup>9</sup> As described more fully below, these rules set forth auction methodology, application procedures, payment and safeguard provisions. In addition, the *Fourth Report and Order* established provisions to ensure that designated entities are afforded a meaningful opportunity to participate in the auction.<sup>10</sup> We adopted an installment payment plan to permit small businesses (including those owned by minorities and women) to pay 80 percent of their winning bid in quarterly installments over the course of the license term.<sup>11</sup> In addition, we established a 25 percent bidding credit for women- and minority-owned businesses. This bidding credit was intended to operate as a discount on the price a qualifying firm would actually have to pay to obtain an IVDS license.<sup>12</sup> The bidding credit was made available for one of the two licenses in each service area (i.e., for either frequency segment A or B).<sup>13</sup> Finally, we implemented a tax credit program to help businesses owned by women and minorities attract start-up capital from non-controlling investors.<sup>14</sup>

5. Utilizing the procedures adopted in the *Fourth Report and Order*, on July 28 and 29,

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<sup>6</sup> 47 U.S.C. § 309(j)(4)(D).

<sup>7</sup> Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Second Report and Order*, PP Docket No. 93-253, 9 FCC Rcd 2348 (1994) (*Second Report and Order*).

<sup>8</sup> Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Second Memorandum Opinion and Order*, PP Docket No. 93-253, 9 FCC Rcd 7245 (1994) (*Second Memorandum Opinion and Order*).

<sup>9</sup> Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Fourth Report and Order*, PP Docket No. 93-253, 9 FCC Rcd 2330 (1994) (*Fourth Report and Order*).

<sup>10</sup> *Id.* at ¶¶ 34-54.

<sup>11</sup> *Id.* at ¶¶ 53-54.

<sup>12</sup> *Id.* at ¶¶ 39-47.

<sup>13</sup> *Id.* at ¶ 39.

<sup>14</sup> *Id.* at ¶¶ 48-52.

1994, we held an auction for IVDS licenses covering 594 MSAs.<sup>15</sup> This auction generated more than \$200 million for the U.S. Treasury and resulted in the award of nearly 94 percent of the licenses to small businesses, including businesses owned by minorities and women. In anticipation of this future auction, we hereby reexamine certain aspects of our auction rules for IVDS. We anticipate that licenses with service areas based on the 428 RSAs<sup>16</sup> will be auctioned in the coming year. At that time, the Commission also intends to reacquire any IVDS licenses where the winning bidders from the previous auction have been found in default.

6. In the *Fifth Report and Order* in this docket (establishing competitive bidding procedures for broadband personal communications services), we stated that the provisions we established for minorities and women are constitutional under the "intermediate scrutiny" standard of review articulated in *Metro Broadcasting, Inc. v. FCC*.<sup>17</sup> On June 12, 1995, the Supreme Court decided in *Adarand* that "all racial classifications . . . must be analyzed by a reviewing court under strict scrutiny."<sup>18</sup> The Court ruled that any federal program that makes distinctions on the basis of race must serve a compelling governmental interest and must be narrowly tailored to serve that interest.<sup>19</sup> The Court overruled *Metro Broadcasting* "to the extent that *Metro Broadcasting* is inconsistent with" *Adarand's* holding.<sup>20</sup>

## IV. SIXTH MEMORANDUM OPINION AND ORDER

### A. Auction Methodology, Payments and Procedures

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<sup>15</sup> "MSAs" refer to "Metropolitan Statistical Areas". See Announcing High Bidders for 594 Interactive Video and Data Service Licenses, Public Notice No. 44160 (Aug. 2, 1994). The MSAs auctioned in IVDS, like the Rural Service Areas discussed *infra*, correspond with cellular radio service areas. See *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 16.

<sup>16</sup> "RSAs" refer to "Rural Service Areas".

<sup>17</sup> 497 U.S. 547, 564-565 (1990). See also Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Fifth Report and Order*, PP Docket No. 93-253, 9 FCC Rcd 5532 (1994) at ¶ 9 (*Fifth Report and Order*). In *Metro Broadcasting*, the Supreme Court ruled that the Commission's minority preference program for mutually exclusive applications for licenses for new radio or television broadcast stations and its distress sale program did not violate the equal protection component of the Fifth Amendment. The Court held that congressionally mandated minority programs (even if not directly remedial in the sense of being designed to compensate individual victims of past governmental or societal discrimination) "are constitutionally permissible to the extent that they serve important governmental objectives within the power of Congress and are substantially related to achievement of those objectives." *Metro Broadcasting v. FCC*, 497 U.S. at 565.

<sup>18</sup> *Adarand*, 115 S.Ct. at 2113.

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

## 1. Establishment of Auction Dates

7. Background. In the *Fourth Report and Order*, the Commission adopted competitive bidding rules for selecting between mutually exclusive applicants for IVDS spectrum. By Public Notices issued on May 23, June 17, and July 5, 1994, we provided additional information concerning the IVDS auctions.<sup>21</sup> In addition, on June 6, 1994, the Commission held an informational auction seminar regarding IVDS licenses.

8. Petition. Phase One argues that, because the Commission may only conduct an auction if there are mutually exclusive applications, it should not have established IVDS auction dates until mutual exclusivity had been determined.<sup>22</sup> Phase One also maintains that interested parties did not have adequate time to plan their competitive bidding strategy for the IVDS auction.<sup>23</sup>

9. Decision. We disagree with Phase One's assertion that the Commission may not establish auction dates or publicize auctions until we have determined that mutual exclusivity exists. While we recognize that we cannot conduct an auction for licenses for which there are no mutually exclusive applications, we note that scheduling and announcing auction dates are no more than preparatory measures. We indicated, in the *Fourth Report and Order*, that in the event the Commission receives only one application that is acceptable for filing for a particular frequency segment, then the pre-scheduled auction would be cancelled.<sup>24</sup> Moreover, we conducted the July 1994 auction for IVDS licenses only after mutual exclusivity had been established in all markets. Thus, we conclude that our pre-auction application procedures ensure that spectrum auctions will be conducted only in those circumstances authorized by the Communications Act.

10. We also disagree with Phase One's allegation that our auction schedule did not provide applicants adequate time to prepare for the IVDS auction. The Commission received more than 500 applications by the June 27, 1994 filing deadline for short-form applications (FCC Form 175). The large number of timely applications we received, along with our outreach efforts to disseminate information to the public about the IVDS auctions, through the initial May 23,

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<sup>21</sup> "Notice and Filing Requirements for the First Auction of IVDS Licenses," Public Notice (May 23, 1994); "First Amendment to Bidder's Information Package and the May 23, 1994 Public Notice Announcing the Auction of Approximately 600 IVDS Licenses," Public Notice (June 17, 1994); "Clarification of the Requirement on Multiple Applicants Being Represented by the Same Bidding Agent at the Auction of Approximately 600 IVDS Licenses," Public Notice (July 5, 1994). *See also* "IVDS Information Packet" (May 1994); "FCC Informational Auction Seminar June 6, 1994," News Release (May 25, 1994); "Answers to Questions from the June 6, 1994 FCC Bidders Seminar for the Auction of IVDS Licenses," Public Notice (June 20, 1994).

<sup>22</sup> Phase One Petition for Reconsideration (filed June 13, 1994) at 2, 5-6 (Phase One Petition). Phase One observes that advertisements for the IVDS auction appeared in the *Wall Street Journal*.

<sup>23</sup> *Id.* at 3-4.

<sup>24</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 21.

1994 Public Notice and subsequent public notices issued during the five week period prior to the filing deadline, evidence that a substantial number of parties found themselves aptly prepared to participate in the IVDS auction. As a result, we find Phase One's contention to be unpersuasive.

## 2. Rules Prohibiting Settlement and Collusion

11. Background. In the *Second Report and Order*, we adopted rules prohibiting collusive conduct in the context of competitive bidding.<sup>25</sup> Specifically, we determined that bidders would be prohibited from discussing the substance of their bids or bidding strategies with other bidders, unless such bidders are members of a bidding consortium or other joint bidding arrangement identified on their short-form application. We also required bidders to identify on their short-form applications all parties with whom they have entered into any consortium arrangements, joint ventures, partnerships or other agreements relating to the competitive bidding process.<sup>26</sup> We also determined that auction applicants would not be permitted to make any ownership changes or changes in the identification of parties to bidding consortia once a short-form application is filed.<sup>27</sup>

12. Petition. ITV argues that our rule prohibiting collusive conduct operates to preclude settlements between mutually exclusive applicants in violation of Section 309 subsections (j)(6)(A) and (E) of the Communications Act and the Commission's policy of allowing settlements.<sup>28</sup> ITV thereby requests that applicants be permitted to communicate with one another following the short-form application deadline to pursue full-market settlements.<sup>29</sup>

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<sup>25</sup> See 47 C.F.R. § 1.2105(c); see also *Second Memorandum Opinion and Order*, 9 FCC Rcd 7245 at ¶¶ 50-53, *erratum*, Mimeo No. 50278 (Oct. 19, 1994).

<sup>26</sup> *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 166.

<sup>27</sup> *Id.* at ¶ 167.

<sup>28</sup> ITV Petition for Reconsideration (filed June 13, 1994) at 4-11 (ITV Petition). Specifically, ITV refers to Section 309(j)(6) of the Communications Act, containing the following rules of construction:

(6) Rules of Construction -- Nothing in this sub-section, or in the use of competitive bidding, shall --

(A) alter spectrum allocation criteria and procedures established by the other provisions of this Act;

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(E) be construed to relieve the Commission of the obligation in the public interest to continue to use engineering solutions, negotiation, threshold qualifications, service regulations, and other means in order to avoid mutual exclusivity in application and licensing proceedings; ...

*Cf.* 47 C.F.R. § 22.131(c)(4).

<sup>29</sup> *Id.* at 11.



13. Decision. We reject ITV's contention that the Commission lacks the authority under the Communications Act to preclude settlements between mutually exclusive applicants for licenses in auctionable services. While the Commission has an established policy of favoring settlements in some contexts, it is within our statutory authority to restrict settlements if we find such agreements would not be in the public interest.<sup>30</sup> At this time, we find that prohibiting settlements after the short form filing deadline between mutually exclusive applicants for the same license in the IVDS competitive bidding process is necessary to deter collusive conduct and ensure a competitive auction, and is thereby in the public interest. Our collusion rules also prevent entities from filing applications solely for the purpose of demanding payment from other bidders in exchange for settlement or withdrawal.

14. Nevertheless, we take this opportunity to clarify certain aspects of our anti-collusion rules.<sup>31</sup> We clarify that the anti-collusion rules apply where one applicant has a common ownership interest with another applicant.<sup>32</sup> Specifically, unless the second applicant is expressly identified as an entity with whom the first applicant has an agreement concerning bidding, these parties may not communicate with each other concerning their bids or bidding strategies. This prohibition holds even where the other bidder is identified on the applicant's short-form application as having a common ownership interest with the applicant.<sup>33</sup> Further, consistent with

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<sup>30</sup> In the broadcast contexts, for example, while we have allowed settlements between applicants for construction permits, such agreements have been significantly restricted in recent years. *See Report and Order*, MM Docket No. 90-263, 6 FCC Rcd 85 (1990), *recon. Memorandum Opinion and Order*, 6 FCC Rcd 2901 (1991) (limiting settlements between mutually exclusive applicants for broadcast construction permits).

<sup>31</sup> 47 C.F.R. § 1.2105(c). *See also Second Memorandum Opinion and Order*, 9 FCC Rcd 7245 at ¶¶ 48-53; In the Matter of Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Fourth Memorandum Opinion and Order*, PP Docket No. 93-253, 9 FCC Rcd 6858 (1994) (*Fourth Memorandum Opinion and Order*) at ¶¶ 47-60; Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Memorandum Opinion and Order*, PP Docket No. 93-253, 9 FCC Rcd 7684 (1994) (*Memorandum Opinion and Order*) at ¶¶ 812; *Public Notice*, "Wireless Telecommunications Bureau Clarifies Spectrum Auction Anti-Collusion Rules," DA 95-2244 (released October 26, 1995).

<sup>32</sup> *Id.* at ¶ 53.

<sup>33</sup> *See Second Memorandum Opinion and Order*, 9 FCC Rcd 7245 at ¶ 53. The Wireless Telecommunications Bureau released a Public Notice clarifying the Commission's anti-collusion rules. *See Public Notice*, Wireless Telecommunications Bureau Clarifies Spectrum Auction Anti-Collusion Rules, DA 95-2244 (Oct. 26, 1995). The anti-collusion rules were further clarified in a November 3, 1996 Order. *See Amendment of Parts 21 and 74 of the Commission's Rules with Regard to Filing Procedures in the Multipoint Distribution Service and in the Instructional Television Fixed Service and Implementation of Section 309(j) of the Communications Act--Competitive Bidding*, Order, DA 95-2292 (rel. Nov. 3, 1995).

We also note that applicants are subject to existing antitrust laws. For example, this prohibits discussions with respect to bid prices between any applicants who have applied for licenses in the same or overlapping geographic license areas. *See United States v. Champion Int'l Corp.*, 557 F.2d 1270 (9th Cir.), 434 U.S. 938 (1977); *c.f., e.g., United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 293 (6th Cir. 1898), *modified and aff'd* 175 U.S. 211 (1899). In addition, agreements between two or more actual or potential competitors to submit collusive, non-competitive or rigged bids are *per se* violations of Section One of the Sherman Antitrust Act, 15 U.S.C. § 1 *et seq.* *See, e.g., United*

the Wireless Telecommunications Bureau's (Bureau) approach in the Broadband PCS C Block auction, amendments to the short-form application must be filed with the Commission within ten business days of any such change.<sup>34</sup>

### 3. Competitive Bidding Methodology

15. Background. In the *Second Report and Order*, we established the criteria to be used in selecting the competitive bidding methodology for each auctionable service. Generally, we concluded that awarding licenses to those parties that value them most highly will promote the rapid development and deployment of new services, and the efficient and intensive use of the spectrum.<sup>35</sup> In the *Fourth Report and Order*, the Commission adopted an oral outcry competitive bidding methodology for auctioning 594 MSA licenses in IVDS. For the remaining RSA licenses, the Commission concluded that a sealed bid competitive bidding mechanism was appropriate. The Commission observed that both methods appear suited to IVDS because they are relatively inexpensive for the Commission to administer and the costs of bidder participation are fairly low. Moreover, we noted that both methods are relatively simple for bidders to understand and generally can be completed quickly.<sup>36</sup> The issue of cost, for both the Commission and the applicants, was an especially important factor in making these choices, because we expected the value of IVDS licenses to be relatively low compared to the value of other auctionable services. We reserved discretion, however, to reconsider this competitive bidding design if, in view of our actual auctions experience, a change appears warranted.<sup>37</sup>

16. Decision. We anticipate that we will auction the remaining IVDS licenses using the oral outcry method. We used this method successfully to auction 594 MSA licenses on July 28 and 29, 1994, and find that auctioning IVDS licenses in this manner continues to serve the public interest. We amend our IVDS rules, however, to permit the use of simultaneous multiple round bidding as well. This method, with its remote bidding capabilities, has been successful in our PCS, Multipoint and/or Multichannel Distribution Service (MDS), and 900 MHz Specialized

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*States v. MMR Corporation (LA)*, 907 F.2d 489 (5th Cir. 1990); *United States v. W.F. Brinkley & Sons Construction Co.*, 783 F.2d 1157 (4th Cir. 1986); *United States v. Finis P. Renest, Inc.*, 509 F.2d 1256 (7th Cir. 1975), *cert. denied*, 423 U.S. 874. Similarly, agreements between actual or potential competitors to divide or allocate territories horizontally in order to minimize competition are *per se* violations of the Sherman Act (*United States v. Topco*, 405 U.S. 596 (1972); *Affiliated Capital Corporation v. City of Houston*, 700 F.2d 226, 236), and such agreements are anticompetitive regardless of whether the parties split a market in which they both do business or whether they merely reserve one market for one and another for the other. See *Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46, 49 (1990).

<sup>34</sup> See *Public Notice*, Qualified Bidders and Bidding Instructions For December 18, 1995 Broadband PCS C Block Auction, Report No. AUC-95-05, Auction No. 5 at 3 (Dec. 8, 1995).

<sup>35</sup> *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 5.

<sup>36</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 11

<sup>37</sup> *Id.* at ¶ 16.

Mobile Radio (900 MHz SMR) auctions. As we continue to gain experience in conducting simultaneous multiple round auctions, the costs associated with this methodology decline. As a result, we reserve the option of using a simultaneous multiple round auction methodology for future IVDS auctions. We delegate authority to the Bureau to announce the type of auction and the procedures by Public Notice.

17. Simultaneous multiple round bidding permits remote bidding from personal computers throughout the country, with resultant flexibility and cost savings for both the public and the Commission.<sup>38</sup> This auction design can also be superior at yielding information to bidders during the course of the auction. The primary drawback to using the design is its cost, although this has decreased as the Commission has gained experience with auctions. Specific procedures are set forth below.

18. Bid Increments. In the event that we use the simultaneous multiple round auction methodology, we will specify minimum bid increments.<sup>39</sup> The bid increment is the amount or percentage by which the bid must be raised above the previous round's high bid in order to be accepted as valid in the current bidding round. The application of a minimum bid increment speeds the auction progress and, along with activity and stopping rules, helps to ensure that the auction closes within a reasonable period of time. Establishing an appropriate minimum bid increment is important in a simultaneous auction with a simultaneous closing rule, because all markets remain open until there is no bidding on any license and a delay in closing one market will delay the closing of all markets.

19. If we elect to use simultaneous multiple round auctions, we will conduct the auction in three stages and start the auction with large bid increments, reducing the increments as bidding activity falls. The minimum bid increment in Stage I of the auction will be 5 percent of the high bid in the previous round or \$.02 per bidding unit, whichever is greater. The Commission will reduce the minimum bid increment as the auction moves through its stages, with a minimum bid increment of the greater of two percent or \$.01 per bidding unit in Stage II, and the greater of one percent or \$.005 per bidding unit in Stage III.<sup>40</sup> The Commission, however, retains the discretion in IVDS auctions to vary the minimum bid increments for individual licenses, or groups of licenses, at any time before or during the course of an auction. The Commission delegates to the

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<sup>38</sup> In the *Fourth Report and Order* we noted that one commenter, ICC, favored sealed (or electronic) bidding over oral bidding because, it argued, some potential bidders could not afford to attend an auction in person. *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 15 & n. 26.

<sup>39</sup> See *Second Report and Order*, 9 FCC Rcd 2348 at ¶¶ 124-126.

<sup>40</sup> In oral or electronic sequential auctions, the auctioneer may, within his or her sole discretion, establish and vary the amount of the minimum bid increments in each round of bidding.

Bureau the authority to exercise such discretion.<sup>41</sup>

20. Stopping Rules. In multiple round auctions, a stopping rule must be established for determining when the auction is over.<sup>42</sup> In simultaneous multiple round auctions, bidding may close separately on individual licenses, simultaneously on all licenses, or a hybrid approach may be used. Under a license-by-license approach, bidding closes on each license after a certain number of rounds pass in which no new acceptable bids are submitted for that particular license. With a simultaneous stopping rule, bidding generally remains open on all licenses until there is no new acceptable bid for any license. This approach provides bidders full flexibility to bid for any license as more information becomes available during the course of the auction, but it may lead to very long auctions unless an activity rule is imposed. Under a hybrid approach, we may use a simultaneous stopping rule (along with an activity rule designed to expedite closure for licenses subject to the simultaneous stopping rule) for the higher value licenses. For lower value licenses, where the loss from eliminating some back-up strategies is less, we may use the license-by-license approach.

21. If we decide to use simultaneous multiple round bidding for the IVDS auction, we intend to use a simultaneous stopping rule. Because of the large number of licenses likely to be auctioned at once, however, we will retain the discretion either to use a hybrid stopping rule or to allow bidding to close individually for these licenses. The specific stopping rule to conclude bidding on IVDS licenses will be announced by Public Notice prior to auction. The Commission also retains the discretion to declare at any point after 40 rounds that the auction will end after some specified number of additional rounds. We believe this number of rounds will ensure that the auction will not close prematurely, while providing bidders with fair assurance that the auction will be conducted as intended.<sup>43</sup> Bids will be accepted only on licenses where the high bid has increased in the last three rounds.<sup>44</sup> This will deter bidders from continuing to bid on a few low value licenses solely to delay the closing of the auction. It will also enable the Commission to end the auction when it determines that the benefits of terminating the auction and issuing licenses exceed the likely benefits of continuing to allow bidding. The Commission will announce by Public Notice the number of remaining rounds and other final bidding procedures. The Commission delegates to the Bureau the authority to exercise such discretion.

22. Duration of Bidding Rounds. In simultaneous multiple round auctions, bidders may need a certain amount of time to evaluate back-up strategies and develop their bidding plans. In

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<sup>41</sup> See Amendment of Part 0 of the Commission's Rules to Reflect a Reorganization Establishing the Wireless Telecommunications Bureau and to Make Changes in the Delegated Authority of Other Bureaus, *Order*, 10 FCC Rcd 12751 (1995); see also 47 C.F.R. § 0.331.

<sup>42</sup> See *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 127.

<sup>43</sup> See *Fifth Report and Order*, 9 FCC Rcd 5532 at ¶ 48.

<sup>44</sup> *Id.* at ¶ 49.

the event we use the simultaneous multiple round auction methodology, we delegate to the Bureau the discretion to vary the duration of the bidding rounds or the interval at which bids are accepted (e.g., run more than one round per day) in order to move the auction toward closure more quickly. The Bureau will announce any changes to the duration of, and intervals between, bidding rounds, either by Public Notice prior to the auction or by announcement during the auction.

23. Activity Rules. As discussed above, in order to ensure that simultaneous auctions with simultaneous stopping rules close within a reasonable period of time and to increase the information conveyed by bid prices during the auction, it is necessary to impose an activity rule to prevent bidders from waiting until the end of the auction before participating. In the *Second Report and Order*, we adopted the Milgrom-Wilson activity rule as our preferred activity rule where a simultaneous stopping rule is used.<sup>45</sup> The Milgrom-Wilson approach encourages bidders to participate in early rounds by limiting their maximum participation to some multiple of their minimum participation level. Bidders are required to declare their maximum eligibility in terms of bidding units, and to make an upfront payment proportional to that eligibility level.<sup>46</sup> In each round, bidders are limited to bidding on licenses encompassing no more than the number of bidding units covered by their upfront payment. Licenses on which a bidder is the high bidder at the end of the withdrawal period in the previous round, as well as licenses on which a new valid bid is placed, count toward this limit. Under this approach, bidders have the flexibility to shift their bids among any license for which they have applied so long as, within each round, the total bidding units encompassed by those licenses does not exceed the total number of bidding units on which they are eligible to bid.

24. Under the Milgrom-Wilson approach, the minimum activity level, measured as a fraction of the bidder's eligibility in the current round, will increase during the course of the auction. Absent waivers (discussed *infra*), a bidder's eligibility (in terms of bidding units) in the current round is determined by the bidder's activity level and eligibility in the previous round. In the first round, however, eligibility is determined by the bidder's upfront payment and is equal to the upfront payment divided by \$.02 per bidding unit.

25. In each round of Stage I, a bidder who wishes to maintain its current eligibility must be active on licenses encompassing at least one-half of the bidding units for which it is eligible. Failure to maintain the requisite activity level will result in a reduction in the amount of bidding units upon which a bidder may be eligible to bid in the next round of bidding (unless an activity rule waiver is used). During Stage I, if bidding activity is below the required minimum level, eligibility in the next round will be calculated by multiplying the current round activity by two (2). Eligibility for each applicant in the first round of the auction is determined by the amount of the upfront payment received and the licenses identified in its auction application. In each round of

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<sup>45</sup> *Second Report and Order*, 9 FCC Rcd 2348 at ¶¶ 144-145.

<sup>46</sup> See discussion of upfront payments at ¶¶ 32-34, *infra*.

Stage II, a bidder who wishes to maintain its current eligibility is required to be active on at least 75 percent of the bidding units for which it is eligible in the current round. During Stage II, if activity is below the required minimum level, eligibility in the next round will be calculated by multiplying the current round activity by four thirds (4/3). In each round of Stage III, a bidder who wishes to maintain its current eligibility must be active on licenses encompassing at least 95 percent of the bidding units for which it is eligible in the current round. In Stage III, if activity in the current round is below 95 percent of current eligibility, eligibility in the next round will be calculated by multiplying the current round activity by twenty nineteenth (20/19). We reserve the discretion to set and, by announcement before or during the auction, vary the requisite minimum activity levels (and associated eligibility calculations) for each auction stage. Retaining this flexibility will improve the Commission's ability to control the pace of the auction and help ensure that the auction is completed within a reasonable period of time.

26. In general, the auction will start in Stage I and move to Stage II if the auction activity level is below 10 percent for three consecutive rounds in Stage I, and move from Stage II to Stage III if the auction activity level is below five percent for three consecutive rounds in Stage II. In no case can the auction revert to an earlier stage. However, the Commission retains the discretion to announce during the course of an auction when, and if, the auction will move from one auction stage to the next. These determinations will be based on a variety of measures of bidder activity including, but not limited to, the auction activity level defined above, the percentage of licenses (measured in terms of bidding units) on which there are new bids, the number of new bids, and the percentage increase in revenue. The Commission delegates to the Bureau the authority to exercise such discretion.

27. Activity Waivers. To avoid the consequences of clerical errors and to compensate for unusual circumstances that might delay a bidder's bid preparation or submission on a particular day, we will provide bidders with five activity rule waivers that may be used in any round during the course of the auction. If a bidder's activity level is below the required activity level a waiver automatically will be applied. That is, if a bidder fails to submit a bid in a round, and its activity level from any standing high bids (high bids at the end of the bid withdrawal period in the previous round) falls below its required activity level, a waiver will be applied automatically. A waiver will preserve current eligibility in the next round, but cannot be used to correct an error in the amount bid. An activity rule waiver applies to an entire round of bidding and not to a particular MSA or RSA service area.

28. Bidders will be afforded an opportunity to override the automatic waiver mechanism when they place a bid, if they intentionally wish to reduce their bidding eligibility and do not want to use a waiver to retain their eligibility at its current level.<sup>47</sup> If a bidder overrides the automatic waiver mechanism, its eligibility will be reduced permanently (according to the formulas specified above), and it will not be permitted to regain its bidding eligibility from a previous round. An automatic waiver invoked in a round in which there are no valid bids will not keep the auction

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<sup>47</sup> See *Fourth Memorandum Opinion and Order*, 9 FCC Rcd 6858 at ¶ 15.

open. Bidders will have the option to enter an activity rule waiver proactively during the bid submission period. Thus, a "proactive" waiver, as distinguished from an automatic waiver, is one requested by the bidder. If a bidder submits a proactive waiver in a round in which no other bidding activity occurs, the auction will remain open.

29. If a simultaneous multiple round auction is employed, the Commission retains the discretion to issue additional waivers during the course of an auction for circumstances beyond a bidder's control and delegates to the Bureau the authority to exercise such discretion. The Bureau also retains the flexibility to adjust, by Public Notice prior to an auction, the number of waivers permitted, or to institute a rule that allows one waiver during a specified number of bidding rounds or during specified stages of the auction.<sup>48</sup>

30. A waiver may be submitted either in the round in which bidding falls below the minimum required level to maintain (for the next round) the same eligibility as in that round, or prior to submitting a bid in the next round. If an activity rule waiver is entered in a round in which no other bidding activity occurs, the auction will remain open.<sup>49</sup> However, an activity rule waiver entered after a round in which no other bidding activity occurs will not reopen the auction. In addition, to help ensure that the auctions are not closed prematurely, we will retain the discretion to keep an auction open even if no new acceptable bids and no proactive waivers are submitted in a single round. In such an instance, the Commission would, in effect, be submitting its own proactive waiver, thus keeping the auction open. At such time, the Commission could also advance to larger bid increments, speeding the pace of the auction.

31. Bid Withdrawal Provisions. If we choose to use a simultaneous multiple round auction methodology, we intend to apply bid withdrawal provisions. In the *Second Report and Order*, the Commission determined that bid withdrawal provisions were needed to discourage insincere bidding.<sup>50</sup> The Commission observed that insincere bidding, whether frivolous or strategic, distorts the price information generated by the auction process and reduces its efficiency.<sup>51</sup> Accordingly, we adopt the bid withdrawal provisions established in the *Second Report and Order*.<sup>52</sup> Pursuant to these rules, any bidder who withdraws a high bid during an auction will be required to reimburse the Commission the amount of the difference between its high bid and the amount of the winning bid the next time the license is offered by the Commission,

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<sup>48</sup> See *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 145.

<sup>49</sup> However, if we determine, based on evidence from experimental and actual auctions, that this is likely to excessively delay the close of an auction or result in other adverse strategic manipulation of an auction, the Bureau may announce by Public Notice prior to a specific auction that submission of a waiver will not keep an auction open under any circumstances.

<sup>50</sup> See *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 147.

<sup>51</sup> *Id.*

<sup>52</sup> See 47 C.F.R. § 1.2104(g)(1).

if this subsequent winning bid is lower than the withdrawn bid. No withdrawal payment will be assessed if the subsequent winning bid exceeds the withdrawn bid. If a license is reoffered by auction, the "winning bid" refers to the high bid in the auction in which the license is reoffered. If a license is reoffered in the same auction, the winning bid refers to the high bid amount, made subsequent to the withdrawal, in that auction. If the subsequent high bidder also withdraws its bid, that bidder will be required to pay an amount equal to the difference between its withdrawn bid and the amount of the subsequent winning bid the next time the license is offered by the Commission. If a license which is the subject of withdrawal is not re-auctioned but is instead offered to the highest losing bidder(s) in the initial auction, the "winning bid" refers to the bid of the highest bidder who accepts the offer. Losing bidders would not be required to accept the offer, *i.e.*, they may decline without penalty. The payment amount will be deducted from any upfront payments or down payments that the withdrawing bidder has deposited with the Commission.<sup>53</sup>

#### 4. Upfront and Down Payments

32. Background. In establishing its auction methodology for IVDS, the Commission set forth several provisions to ensure that winning bidders have the resources needed to obtain their licenses and construct their systems and to discourage insincere bidding. In the *Fourth Report and Order*, we required applicants to show a cashier's check in the amount of \$2,500 for each five licenses sought in order to obtain a bidding number and participate in the auction. Immediately following the auction, winning bidders were required to submit a \$2,500 upfront payment for every five licenses won.<sup>54</sup> We anticipated that this amount would ensure that only serious, qualified applicants would be eligible to bid at auction. In addition, we required winning bidders to make a substantial down payment within five business days after the close of bidding. Generally, we required that the down payment be sufficient to bring the winning bidder's total deposit with the Commission up to 20 percent of the amount bid.<sup>55</sup> Small business applicants were permitted to pay 10 percent at that time and the remaining 10 percent within five days of the grant of the license.

33. Petition. ITV requests that the Commission refund upfront payment amounts to the extent that they not only cover, but exceed, the required down payment. ITV maintains that this

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<sup>53</sup> But see *Atlanta Trunking Associates, Inc. v. MAP Wireless L.L.C. Requests to Waive Bid Withdrawal Payment Provisions*, FCC 96-203, *Order*, (rel. May 3, 1996)(summarized in 61 Fed. Reg. 25,807 (May 23, 1996)), *recon. pending* ("*Atlanta Trunking*"). The *Atlanta Trunking* guidelines were formally incorporated into and adopted by a *Report and Order* which amended Section 24.704 of the Commission's rules to reflect the changes. See *Report and Order*, FCC 96-278 (rel. June 24, 1996).

<sup>54</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 24. See also the detailed discussion *infra* in ¶¶ 76-77 on increasing the upfront payment amounts.

<sup>55</sup> *Id.*



policy would ensure that winning bidders are not penalized by prevailing with a low bid. ITV alleges that this modification is especially important to applicants that qualify as a small business, who need to conserve their financial resources for other auctions, and when the Commission cannot pay interest on collected funds.<sup>56</sup>

34. Decision. We grant ITV's petition on this issue. We agree with ITV that winning bidders should not be penalized because their winning bid was lower than the amount the upfront payment would suggest. The Commission will issue a refund to any qualified applicant after determining that no bid withdrawal or default payments are owed. Due to administrative constraints, however, we will not honor requests that any excess amount be retained and applied toward later payments or obligations. Additional instructions for obtaining a refund will be provided in a Bidder Information Package prior to auction.

## 5. Default Provisions

35. Background. In the *Fourth Report and Order*, we adopted default payments to discourage insincere bidding and to compensate the government for the cost of reauctioning a license. Specifically, we determined that the defaulting auction winner would be assessed an additional payment of three percent of the subsequent winning bid or three percent of its own bid, whichever is less.<sup>57</sup>

36. Petition. ITV requests that, where the new bid on a license (upon reauction) exceeds the defaulting applicant's bid by 3 percent or more, no default payment be applied.<sup>58</sup> In the event that the subsequent bid exceeds the defaulting bid by less than 3 percent, ITV requests that the defaulting applicant should only be responsible for payment of the difference between the subsequent winning bid and 103 percent of the defaulting applicant's bid.<sup>59</sup> ITV maintains that this proposal will prevent any windfall to the U.S. Treasury.<sup>60</sup>

37. Decision. We believe that our existing default provisions serve an important purpose by helping to deter insincere or speculative bidding, and providing an incentive for bidders wishing to withdraw their bids to do so before bidding ceases. In the *Second Report and Order*, we observed that it is appropriate to create such an incentive because a withdrawal that occurs after

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<sup>56</sup> ITV Petition at 15-17.

<sup>57</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 29.

<sup>58</sup> ITV Petition at 14.

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

an auction closes (default) is likely to be more harmful than one that occurs before closing.<sup>61</sup> We noted, for example, that default reduces the likelihood that licenses will be assigned to those who value them the most and imposes additional costs on the government. Therefore, we determined that an additional 3 percent payment would discourage bidders from defaulting on licenses won at auction. We continue to believe that this amount is appropriate and will reasonably compensate the government for costs associated with reaucting the license. Thus, we reject ITV's proposal.

## B. Designated Entity Provisions

38. Background. In the *Fourth Report and Order*, we established several special provisions to ensure that designated entities, *i.e.*, small businesses, rural telephone companies, and businesses owned by members of minority groups and women, are given the opportunity to participate both in the competitive bidding process for, and in the provision of, IVDS.<sup>62</sup> Our rules provide that on one of the two licenses in each market, a 25 percent bidding credit would be awarded to a winning bidder that is a business owned by women or minorities.<sup>63</sup> We declined to provide bidding credits to rural telephone companies, however, because we concluded that the relatively modest build-out costs for systems in this service would make such special provisions unnecessary to ensure that they had the opportunity to participate in the provision of IVDS offerings to rural areas.<sup>64</sup> We also made tax certificates available to initial investors in minority and women-owned businesses, and to licensees that transfer their authorizations to minority and women-owned enterprises.<sup>65</sup> Finally, because installment payments are an effective way to promote the participation of designated entities and to distribute licenses and services among geographic areas, and because use of IVDS spectrum is very likely to match the business objectives of *bona fide* small businesses, we allowed small businesses to pay for their licenses using installment payments.<sup>66</sup>

39. Also, to ensure that our special provisions for designated entities would benefit only the parties to whom they were directed, we adopted "unjust enrichment" provisions designed to discourage trafficking in licenses obtained using these special provisions.<sup>67</sup> For example, the unjust enrichment provisions require reimbursement of the bidding credit plus interest when the

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<sup>61</sup> *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 154.

<sup>62</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶¶ 34-54.

<sup>63</sup> See 47 C.F.R. §§ 95.816(d)(1).

<sup>64</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at n.66.

<sup>65</sup> *Id.* at ¶¶ 48-52.

<sup>66</sup> *Id.* at ¶¶ 53-54; *Second Report and Order*, 9 FCC Rcd at ¶¶ 231-240.

<sup>67</sup> See 47 C.F.R. §§ 1.2111, 95.816(e).

licensee assigns or transfers the license to a business not owned by minorities and/or women.<sup>68</sup> In addition, we require small business licensees to pay back the full amount of the remaining principal balance upon transfer or assignment of a license to a non-qualifying entity.<sup>69</sup>

## 1. Bidding Credits

40. Petition. ITV requests that a bidding credit be made available for both licenses in each IVDS service area. ITV asserts that we did not adequately explain why we restricted the use of bidding credits to one license per service area, and that any interest in "maximizing" auction revenue would be contrary to statutory authority.<sup>70</sup>

41. Decision. We grant ITV's petition on this issue. In the *Fourth Report and Order*, we stated that providing bidding credits in the IVDS auctions was "necessary to provide [the pertinent] designated entities with a significant enough advantage to ensure their ability to compete successfully for some IVDS licenses."<sup>71</sup> We note, however, that the Commission is not required to provide all potential special provisions to all designated entities in all auction contexts. We also note, contrary to ITV's assertions, that the Commission did not limit the application of bidding credits to only half of the available licenses solely to maximize auction revenues, but rather considered many other factors. We chose to make bidding credits available to only half of the available licenses, rather than all of them, because we believed that this substantial level of assistance, coupled with the special provision of tax certificates, fulfilled our statutory mandate to ensure that businesses owned by minorities and/or women would have a meaningful opportunity to participate in the competitive bidding process for, and in the provision of, IVDS offerings. We note that these provisions achieved a high degree of designated entity participation in the initial IVDS auction. Of the 594 licenses, 195 (32.8%) were won by bidders claiming minority-owned status, 282 (47.5%) by bidders claiming woman-owned status, and 557 (93.8%) by bidders claiming small business status. Since that time, however, the tax certificate program has been discontinued by Congress,<sup>72</sup> and, as discussed *infra*, we are reconsidering the eligibility criteria for

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<sup>68</sup> See *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 30. The payment equals the amount of the bidding credit plus interest at the rate imposed for installment financing at the time the license was awarded, and must be paid before the assignment or transfer will be permitted. The amount of the payment is reduced over time: a transfer or assignment in the first two years of the license term results in a forfeiture of 100 percent of the value of the bidding credit; during year three, of 75 percent of the bidding credit; in year four, of 50 percent; in year five, of 25 percent; and thereafter, no forfeiture is assessed.

<sup>69</sup> See *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 36; 47 C.F.R. § 1.2110(c).

<sup>70</sup> ITV Petition at 11-13.

<sup>71</sup> *Fourth Report and Order* at ¶ 39.

<sup>72</sup> H.R. 831, 104th Cong. 1st Sess. § 2. As a result of this action by Congress, we are compelled to eliminate the specific tax certificate provision in our IVDS rules. We have therefore eliminated former Section 95.816(d)(2) of the rules, 47 C.F.R. § 95.816(d)(2), and have redesignated the remainder of Section 95.816(d) as indicated in the Appendix,

bidding credits in the IVDS context in light of the Supreme Court's recent decision in *Adarand*. Accordingly, to the extent we retain bidding credits for IVDS, we will provide bidding credits for both licenses in each service area. In view of the discontinuation of the tax certificate program, we believe that extending the bidding credit to both licenses is appropriate to increase the participation opportunities available for designated entities.<sup>73</sup>

## 2. Tax Certificates

42. We eliminate the tax certificate program available to investors in women- and minority-owned firms. We adopted the tax certificate program in the *Fourth Report and Order* pursuant to authority granted in 26 U.S.C. § 1071.<sup>74</sup> Congress has since repealed Section 1071.<sup>75</sup> As a result, we are compelled to eliminate the tax certificate provision in our IVDS rules.

## 3. Unjust Enrichment Provisions

43. Petition. ITV asserts that the unjust enrichment provision for the transfer of a license obtained using bidding credits should not apply when the license is assigned or transferred at a loss. ITV also asserts that, when the license is profitably assigned or transferred, the forfeiture should be based on profits directly attributable to the license, rather than on the government's cost in providing the bidding credit.<sup>76</sup>

44. Decision. We deny ITV's petition on this issue. We do not believe that the unjust enrichment provisions should take into account the profits or losses of particular businesses. The recapture provisions are designed not only to repay the government for the cost of the benefit conferred, but also to ensure that the special provisions we adopted for designated entities benefit the parties to whom they were directed. Special treatment of designated entities is intended to further the statutory policy of ensuring that these entities have the opportunity to participate in spectrum-based services. The repayment provisions we adopted help to promote the long-term holding of licenses by those parties intended to be benefitted by the bidding credit and installment payment provisions.

## 4. Rural Telephone Companies

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*infra*.

<sup>73</sup> See *Fourth Report and Order* at ¶ 34 (statutory goals described). These include promoting economic opportunity and competition, and disseminating licenses among a wide variety of applicants.

<sup>74</sup> *Fourth Report and Order* at ¶¶ 48-52.

<sup>75</sup> H.R. 831, 104th Cong. 1st Sess. § 2.

<sup>76</sup> ITV Petition at 17-19.

45. Petitions. Petitioners RCA and USIN request that rural telephone companies be provided all the special provisions extended to small businesses and businesses owned by women or minorities.<sup>77</sup> They assert that the Communications Act requires that special provisions be provided to rural telephone companies, and that, without bidding credits and other special provisions, it is unlikely that IVDS offerings will be available in rural areas.<sup>78</sup> They further assert that it will take more than build-out capability for rural telephone companies to provide IVDS offerings. They maintain that financial ability is required to obtain the license at auction in the first place.<sup>79</sup>

46. Decision. We deny the petitions of RCA and USIN on this issue. As noted *supra*, the Commission has discretion to tailor the use of special provisions as necessary for each particular service.<sup>80</sup> For IVDS, we expect that the cost of winning licenses, and subsequently building-out systems, will be relatively modest compared to the costs associated with other services subject to auctions. USIN notes that the *Fourth Report and Order* lacks discussion of the expected actual build-out costs of IVDS systems and the economic characteristics of rural telephone companies.<sup>81</sup> While we cannot yet determine with precision any average cost figures for building and operating an IVDS system, we are familiar with the technical and operational parameters of the service,<sup>82</sup> and believe our assumption is reasonable that build-out costs will be modest relative to such costs for other auctionable services. In addition, we have previously assessed the economic characteristics of rural telephone companies in this proceeding.<sup>83</sup> As a result, we expect that rural telephone companies, even without special provisions, will be able to compete effectively both during the auction and in providing service.

47. With respect to bidding credits, as discussed *infra*, we are proposing to eliminate bidding credits for minority and women-owned businesses and extend a 25 percent bidding credit to small businesses only.<sup>84</sup> A rural telephone company would be eligible for the bidding credit to the extent that it also qualifies as a small business. We also affirm our decision not to provide installment payments for those rural telephone companies that are not also small businesses. We

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<sup>77</sup> RCA Petition for Reconsideration (filed June 13, 1994) (RCA Petition); U.S. Intelco Networks, Inc. Petition for Reconsideration (filed June 13, 1994) (USIN Petition).

<sup>78</sup> RCA Petition at 1-2; USIN Petition at 3-6.

<sup>79</sup> USIN Petition at 4-5; RCA Petition at 5-6.

<sup>80</sup> See ¶ 41, *supra*.

<sup>81</sup> USIN Petition at 4 n. 4, 5.

<sup>82</sup> See *Report and Order*, 7 FCC Rcd at 1633-41.

<sup>83</sup> See *Second Report and Order* at 2397; *Second Memorandum Opinion and Order* at 7256-58.

<sup>84</sup> See ¶¶ 61-67 and 72-75, *infra*.

continue to believe that qualification for installment payments should be limited to businesses that qualify as small.<sup>85</sup>

48. Further, we anticipate that rural areas will be served despite the lack of special provisions for rural telephone companies, because other companies can also serve these areas at relatively low cost. While rural telephone companies possess infrastructure that might place them initially at an advantage over other applicants intending to serve rural areas, they do not, in the IVDS context, require an additional advantage in the form of a separate special provision before it is economically advantageous for them to serve rural customers. Whether or not we establish special provisions in this context is not why rural telephone companies will elect to provide or not provide service to these rural areas. Therefore, consistent with the *Fourth Report and Order*, we deny RCA's and USIN's request that we adopt special provisions specifically for rural telephone companies.

### C. Miscellaneous

49. Audits. Since the initial IVDS auction, we have revised the short-form application to place applicants on notice of the Commission's authority to audit licensees and license applicants.<sup>86</sup> We believe the use of audits and other enforcement tools is necessary to maintain the integrity of the self-certification process we have used in our designated entity provisions. We have specified this authority in our revised IVDS rules.

50. Long-Form Application. While IVDS applicants have previously provided their financial information by filing Form 574 as their long-form application, we now require that they use Form 600.<sup>87</sup> While Form 600 contains certain instructions that IVDS applicants would be instructed to ignore, it is a more complete form than the current Form 574.

51. Divestiture Provisions. In establishing rules for IVDS, we concluded that the best way to promote competition in the IVDS marketplace is to make at least two licenses available in each market.<sup>88</sup> Our rules therefore prohibit an IVDS licensee from acquiring an interest in another IVDS license in the same service area where it is licensed.<sup>89</sup> The Interactive Television Association (ITA) requests that the Commission initiate a rule making proceeding to eliminate this

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<sup>85</sup> *Fourth Report and Order*, 9 FCC Rcd at ¶¶ 53-54 .

<sup>86</sup> See Public Information Collection Requirement Submitted to Office of Management and Budget for Review, 59 Fed. Reg. 63803 (Dec. 9, 1994).

<sup>87</sup> See Notice of Public Information Collections Submitted to OMB for Review and Approval, 61 Fed. Reg. 3699 (Feb. 1, 1996).

<sup>88</sup> *Notice of Proposed Rule Making*, 6 FCC Rcd 1368, 1371 (1991).

<sup>89</sup> See 47 C.F.R. § 95.813(b)(2).

ownership restriction and permit one licensee to own both licenses in a market.<sup>90</sup> ITA maintains that, in view of several telephone and cable companies' interest in interactive television, these rules are no longer needed to promote competition.<sup>91</sup> We decline to grant ITA's petition for rule making at this time. We observe that the interactive television marketplace is in a relatively early state of competition. Moreover, allowing a single entity to acquire both licenses in a service area would limit the opportunity for other potential competitors to emerge. Such a result is inconsistent with Congress' mandate to facilitate the dissemination of licenses among a wide variety of applicants.<sup>92</sup>

52. On our own motion, we also clarify that, where unintended common attributable ownership interests exist between two license winners in an IVDS service area, an applicant will be permitted to divest itself of the prohibited common ownership within 90 days after license grant. Assuming that the applicant is otherwise qualified, the Commission will conditionally grant the license if the winning applicant has submitted a signed statement with its long-form application stating its intent to divest. The licensee must then certify its compliance when timely achieved. In addition, in the event that a licensee seeks to bid on another license in its market at a future auction, it may request a waiver of the common ownership prohibition to bid on the other license. If the licensee then wins the second license, the licensee must divest itself of its existing license within 90 days of the grant of the second and is responsible for all penalty or other amounts that result from these transactions. Any licensee desiring such a waiver should submit its statement and request as an attachment to its short-form application.

## V. FURTHER NOTICE OF PROPOSED RULE MAKING

### A. Treatment of Designated Entities

#### 1. Meeting the *Adarand* Standard

53. Background. In the *Fourth Report and Order*, we established several special provisions to ensure that designated entities, *i.e.*, small businesses, rural telephone companies, and businesses owned by members of minority groups and women, are given the opportunity to participate both in the competitive bidding process for, and in the provision of, IVDS service.<sup>93</sup> Among other provisions, our rules provided that on one of the two licenses in each market, a 25

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<sup>90</sup> ITA Petition for Rulemaking, RM 8551 (filed Oct. 21, 1994). Three letters were received, and they generally support ITA's request. Letter from John D. Elliott (Nov. 14, 1994); Letter from George C. Dick (Nov. 16, 1994); Letter from Cyrus K. Dam (Nov. 19, 1994).

<sup>91</sup> *Id.* at 2-4.

<sup>92</sup> 47 U.S.C. § 309(j)(3)(B).

<sup>93</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶¶ 34-54.

percent bidding credit would be awarded to a winning bidder that is a business owned by women or minorities.<sup>94</sup>

54. The standard of review applied to federal programs designed to enhance opportunities for racial minorities at the time our IVDS rules were adopted was an intermediate scrutiny standard. As the Supreme Court stated in *Metro Broadcasting, Inc. v. FCC*:

[B]enign race-conscious measures mandated by Congress -- even if those measures are not "remedial" in the sense of being designed to compensate victims of past governmental or societal discrimination -- are constitutionally permissible to the extent that they serve important governmental objectives within the power of Congress and are substantially related to achievement of those objectives.<sup>95</sup>

55. In *Adarand*, the Supreme Court invalidated the intermediate scrutiny standard for federal race-based programs. The Court held that all racial classifications, imposed by any federal, state or local government actor, must be analyzed by a reviewing court under strict scrutiny. In other words, such classifications are constitutional only if they are narrowly tailored to further a compelling governmental interest.<sup>96</sup> Moreover, as the Court made clear in *Adarand*, a strict scrutiny standard of review will be applied even if the racial classifications are well motivated or "benign."<sup>97</sup>

56. Application of the two-prong strict scrutiny standard of review to provisions designed to encourage minority participation in IVDS requires the Commission to show: (1) a compelling governmental interest exists for taking race into account in licensing allocation decisions, and (2) the provisions in question are narrowly tailored to further the compelling governmental interest established by the record and findings.<sup>98</sup> *Adarand* offers little guidance regarding the specific requirements of this test. However, other cases, such as *Richmond v. J.A. Croson Co.*,<sup>99</sup> provide us with some indications of the type of record necessary to meet the strict scrutiny standard.

57. In *Croson*, the Supreme Court applied strict scrutiny to invalidate as unconstitutional a municipality's partial set-aside for minority-owned businesses. The Court held that remedying past discrimination constitutes a compelling interest, whether the discrimination was committed by

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<sup>94</sup> See 47 C.F.R. §§ 95.816(d)(1).

<sup>95</sup> *Metro Broadcasting*, 497 U.S. at 564-65.

<sup>96</sup> *Adarand*, 115 S. Ct. at 2113.

<sup>97</sup> *Id.* at 2112.

<sup>98</sup> *Id.* at 2113.

<sup>99</sup> *Croson*, 488 U.S. 469 (1989).



the government or by private actors within its jurisdiction.<sup>100</sup> Other courts have also held remedial measures -- those intended to compensate for past discrimination -- to be compelling governmental interests.<sup>101</sup> In *Croson*, however, the Court made clear that an interest in remedying general societal discrimination could not be considered compelling because a "generalized assertion" of past discrimination "has no logical stopping point" and would support unconstrained uses of racial classifications.<sup>102</sup> Whether other objectives for race-based measures rise to the level of a compelling governmental interest is unclear. However, in a plurality opinion issued before *Adarand*, the Supreme Court indicated that non-remedial measures aimed at fostering ethnic diversity could satisfy the compelling interest requirement of strict scrutiny.<sup>103</sup>

58. The Supreme Court in *Croson* noted the high standard of evidence required for the government to establish a compelling interest. It stated that the government must demonstrate a "strong basis in evidence for its conclusion that remedial action was necessary" and that such evidence should approach "a prima facie case of a constitutional or statutory violation of the rights of minorities."<sup>104</sup> Other courts, in cases decided after *Croson*, have held that statistical evidence can be probative of discrimination in the remedial setting, and that anecdotal evidence can buttress statistical evidence.<sup>105</sup>

59. As indicated above, once a compelling governmental interest is established, narrow tailoring, the second prong of the strict scrutiny test, must also be shown. This requirement is intended to ensure "that the means chosen `fit' [the] compelling goal so closely that there is little or no possibility that the motive for the classification was illegitimate racial prejudice or stereotype."<sup>106</sup> The Court in *Croson* required that the government's remedial actions be narrowly tailored "to break down a pattern of deliberate exclusion" and stated that broader relief could be justified only on the basis of "evidence of a pattern of individual discriminatory acts . . . supported

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<sup>100</sup> *Id.* at 491-93.

<sup>101</sup> See, e.g., *Associated General Contractors v. Coalition for Economic Equity*, 950 F.2d 1401, 1413 (9th Cir. 1991), *cert. denied*, 503 U.S. 985 (1992); *O'Donnell Construction Co. v. District of Columbia*, 963 F.2d 420 (D.C. Cir. 1992); *Cone Corp. v. Hillsborough County*, 908 F.2d 908, 913 (11th Cir. 1990), *cert. denied*, 498 U.S. 983 (1990); *Milwaukee County Pavers Ass'n v. Fiedler*, 922 F.2d 419, 421-22 (7th Cir. 1991), *cert. denied*, 111 S.Ct. 2261 (1991)

<sup>102</sup> *Croson*, 488 U.S. at 498 (quoting *Wygant v. Jackson Board of Education*, 476 U.S. 267, 275 (1986)).

<sup>103</sup> See *Regents of the University of California v. Bakke*, 438 U.S. 265 (1978).

<sup>104</sup> *Croson*, 488 U.S. at 500.

<sup>105</sup> See, e.g., *Peightal v. Metropolitan Dade County*, 26 F.3d 1548, 1556 (11th Cir. 1994) (statistical evidence constitutes requisite "strong basis in evidence"); *Coral Construction Co. v. King County*, 941 F.2d 910, 919 (9th Cir. 1991) *cert. denied*, 502 U.S. 1033 (1992) (convincing anecdotal and statistical evidence can be "potent").

<sup>106</sup> *Croson*, 488 U.S. at 493.

by appropriate statistical proof. . .<sup>107</sup> Different factors have been used by courts to determine, under a strict scrutiny standard, whether a program is narrowly tailored. These include the following: (1) whether race-neutral measures were considered before adopting race-conscious measures;<sup>108</sup> (2) the scope of the program, and whether it contains a waiver mechanism that facilitates narrowing of that scope;<sup>109</sup> (3) the comparison of any numerical target to the number of qualified minorities in the relevant sector;<sup>110</sup> (4) the duration of the program, and whether it is subject to periodic review;<sup>111</sup> (5) the manner in which race is considered, whether as one factor among several or as determinative;<sup>112</sup> and (6) the degree and type of burden on non-minorities.<sup>113</sup>

60. An intermediate scrutiny standard of review currently applies to gender-based measures.<sup>114</sup> Under this standard, a gender-based provision is constitutional if it serves an important governmental objective and is substantially related to achievement of that objective. The Supreme Court has not addressed constitutional challenges to federal gender-based programs since *Adarand*. However, the Supreme Court recently upheld a constitutional challenge to a state gender-based program in *United States v. Commonwealth of Virginia* ("VMI")<sup>115</sup> and reaffirmed the application of an intermediate standard of review to gender-based measures. In *VMI*, the Court first indicated that parties defending their gender-based governmental action must demonstrate an "exceedingly persuasive justification" for their action, then stated that the parties must show at least that the challenged classification serves important governmental objectives and that the discriminatory means employed are substantially related to the achievement of those objectives.<sup>116</sup>

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<sup>107</sup> *Id.* at 509.

<sup>108</sup> See *Adarand*, 115 S.Ct. at 2118; *Croson*, 488 U.S. at 507.

<sup>109</sup> See *Metro Broadcasting*, 497 U.S. at 622 (O'Connor, J., dissenting).

<sup>110</sup> See *Croson*, 488 U.S. at 501-02 (finding that the percentage figure used by the government to determine its minority subcontracting requirement, which was calculated in part based on the African-American population of Richmond, was improper because its usage relied on the assumption that minorities choose trades in direct proportion to their representation in the local population).

<sup>111</sup> See *Fullilove v. Klutznick*, 448 U.S. 448, 513 (Powell, J. concurring) (1980).

<sup>112</sup> See *Podberesky v. Kirwan*, 38 F.3d 147 (4th Cir 1994), *cert. denied*, 115 S. Ct. 2001 (1995).

<sup>113</sup> See *Johnson v. Transportation Agency*, 480 U.S. 616, 638 (1987).

<sup>114</sup> See, e.g., *Ensley Branch, NAACP v. Seibels*, 31 F.3d 1548, 1579-80 (11th Cir. 1994); *Contractors Association v. City of Philadelphia*, 6 F.3d 990, 1009-10 (3d Cir. 1993); *Lamprecht v. FCC*, 958 F.2d 382, 391 (D.C. Cir. 1992); *Coral Construction Co. v. King County*, 941 F.2d 910, 930-31 (9th Cir. 1991) *cert. denied*, 502 U.S. 1033 (1992).

<sup>115</sup> *United States v. Commonwealth of Virginia*, 1996 WL 345786 (United States Supreme Court, June 26, 1996).

<sup>116</sup> *VMI*, 1996 WL 345786 at 11 and 12.

61. Discussion. The evidence supporting our gender- and race-based provisions cited in the *Fourth Report and Order* primarily shows: (1) broad discrimination against racial groups and women by lenders; and (2) underrepresentation of these groups as owners and employees in the communications industry.<sup>117</sup> At present, we believe that the record is insufficient to demonstrate a compelling interest under the strict scrutiny standard to support the race-based incentive programs of IVDS because it reflects primarily generalized assertions of discrimination. *Adarand* and *Croson* make clear that only a record of discrimination against a particular racial group would support remedial measures designed to help that group. Therefore, we believe that a record of discrimination against minorities in general is not sufficient. Specific evidence of discrimination against particular racial groups would be required to support a rule for any group. Our rules define minority group members to include Blacks, Hispanics, American Indians, Alaskan Natives, Asians, and Pacific Islanders.<sup>118</sup> Although we have general evidence of discrimination against certain racial groups, none of the evidence we have appears to satisfy the strict scrutiny standard.

62. Thus, we tentatively conclude that our present record in support of our race-based IVDS provisions is insufficient to satisfy strict scrutiny. We seek comment on our tentative conclusion. We also request comment on whether our IVDS provisions promote a compelling governmental interest and, more particularly, whether compensating for discrimination in lending practices and in practices in the communications industry constitutes such an interest. We also ask interested parties to comment on nonremedial objectives that could be furthered by the minority-based provisions of our IVDS rules and whether they could be considered compelling governmental interests, such as increased diversity in ownership and employment in the communications industry or increased industry competition. In commenting, we ask parties to submit statistical data, personal accounts, studies, or any other data relevant to the entry of specific racial groups into the field of telecommunications. Examples of relevant evidence could include discrimination against minorities trying to obtain FCC licenses for auctioned or non-auctioned spectrum; discrimination against minorities seeking positions of ownership or employment in communications or related businesses; discrimination against minorities attempting to obtain capital to start up or expand a telecommunications enterprise, including terms and conditions; and discrimination against minorities operating telecommunications businesses, including treatment by vendors, FCC licensees, and suppliers.

63. We also ask those parties who conclude that our race-based provisions serve a compelling governmental interest to comment on whether the provisions are narrowly tailored to serve that interest. Are these provisions sufficiently narrow in scope? Do they unduly burden non-minorities?<sup>119</sup> Would race-neutral measures further the same interests and achieve the same

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<sup>117</sup> *Fourth Report and Order*, 9 FCC Rcd at 2337-39.

<sup>118</sup> 47 C.F.R. §24.720(i).

<sup>119</sup> *See Johnson v. Transportation Agency*, 480 U.S. 616, 638 (1987).

objectives as race-conscious measures?<sup>120</sup>

64. In addition, we also tentatively conclude that the present record in support of our gender-based IVDS rules may be insufficient to satisfy intermediate scrutiny. We seek comment on our tentative conclusion. We also seek comment on whether there are remedial or nonremedial goals that would satisfy the "important governmental objective" requirement of the intermediate scrutiny standard such as, for example, increased participation of women in the FCC-licensing process for auctioned spectrum. Are our gender-based IVDS rules "substantially related" to the achievement of such objectives? Just as we requested above, in addressing evidence to support IVDS race-based provisions, we ask parties to submit statistical data, personal accounts, studies, or any other data relevant to the entry of women into the field of telecommunications.

65. We also are interested in supplementing the current record to support race- and gender-based provisions in our other rules. In this regard, the Commission initiated a comprehensive rule making proceeding to explore market barriers to women- and minority-owned businesses, as well as small businesses, pursuant to Section 257 of the Communications Act.<sup>121</sup> The record created in response to this Notice will also be incorporated into that Docket.

66. We undertake this effort to support our auction rules because we are committed to fulfilling the Congressional mandate to provide opportunities for women- and minority-owned businesses through the competitive bidding process. We believe, however, that marshalling sufficient evidence to satisfy the strict scrutiny standard of review now applicable to federal race-based programs may be a time-consuming process, and we are mindful that we may not fulfill our other obligations under Section 309(j) if we delay the award of IVDS licenses until that process is complete.

67. We note that the high number of defaulting bidders in the initial IVDS auction, combined with the delay in auctioning off the RSA licenses, has caused a significant delay in awarding IVDS licenses. This delay has hurt businesses that are interested in developing competitive IVDS. In addition, where one MSA bidder has defaulted, the second winning bidder has had a significant head start over the ultimate winner of the first license in providing service. Given that we authorized two licenses per service area in an attempt to have both licensees make service available in the near future, such an advantage was not contemplated when we established our rules authorizing reauctioning of licenses. We also believe that both Congress and consumers expect us to promote the rapid development of IVDS. Balancing our obligation to provide opportunities for women- and minority-owned businesses to participate in spectrum-based

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<sup>120</sup> See *Adarand*, 115 S.Ct. at 2118; *Croson*, 488 U.S. at 507.

<sup>121</sup> See Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Businesses, *Notice of Inquiry*, GN Docket No. 96-113, FCC 96-216 (rel. May 21, 1996), 11 FCC Rcd 6281, 61 Fed. Reg. 33066 (June 26, 1996) (*Market Entry Notice of Inquiry*).

services against our statutory duties to facilitate the rapid delivery of new services to the American consumer and promote efficient use of the spectrum, we tentatively conclude that we should not contribute any further delays to the IVDS auction by postponing the auction to adduce sufficient evidence to support our race- and gender-based IVDS provisions. While we could proceed with the IVDS auction under the current rules, we tentatively conclude that this course of action would not serve the public interest because it may result in litigation that would delay the auction, the dissemination of additional IVDS licenses, and, ultimately, the introduction of competition.<sup>122</sup> As a result, we tentatively conclude that we will adopt race and gender neutral provisions, but continue to maintain the provisions for small businesses which we believe adequately benefit most of the businesses owned by minorities and/or women. We believe these proposed changes will enable us to meet our Congressional-mandate and proceed as expeditiously as possible to auction the remaining IVDS licenses. We seek comment on these tentative conclusions.

## 2. Special Provisions for Designated Entities

### a. Small Business Definition

68. **Background.** In the *Second Report and Order* we adopted the Small Business Administration's (SBA) definition of small business for our generic auction rules.<sup>123</sup> This definition requires the entity to demonstrate that, together with its affiliates, its net worth is no more than \$6 million, and its annual profits are no more than \$2 million for the previous two years.<sup>124</sup> In the *Fourth Report and Order* we determined that these definitions should apply to applicants for IVDS auctions.<sup>125</sup> Since that time, however, we have defined small business for other services based on the gross revenues of the applicant and its affiliates for the preceding three years.<sup>126</sup>

69. **Discussion.** We propose to define small businesses based on gross revenues for the preceding three years. Specifically, we propose to define a small business as an entity whose average gross revenues for each of the preceding three (3) years do not exceed \$15 million. Additionally, we propose to define a very small business (as discussed later in connection with the tiered bidding credits) as an entity with less than an average of \$3 million in gross revenues in

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<sup>122</sup> *Omnipoint*, slip op. at 17.

<sup>123</sup> *Second Report and Order*, 9 FCC Rcd 2348 at ¶ 271.

<sup>124</sup> *Id.*

<sup>125</sup> See 47 C.F.R. § 95.816(d).

<sup>126</sup> See 47 C.F.R. § 24.720 (broadband PCS); 47 C.F.R. § 24.320 (narrowband PCS); 47 C.F.R. § 90.814(b)(1) (900 MHz SMR); 47 C.F.R. § 90.912(b) (800 MHz SMR).

each of the last three (3) years. We believe that a company's gross revenues is a more accurate indicator of its size than is its net worth or annual profits.<sup>127</sup> A gross revenues test is a clear measure for determining the size of a business and is an established method of determining size eligibility for various types of federal programs that aid small businesses.<sup>128</sup> Moreover, we observe that this approach is consistent with our approach in 900 MHz SMR.<sup>129</sup> Commenters are invited to address whether the Commission should modify its small business definition and calculate small business eligibility based on gross revenues, rather than net worth and annual profits. Commenters should discuss what gross revenues threshold is appropriate for defining small business in the IVDS context.

70. We also propose a five percent attribution threshold for purposes of determining eligibility as a small business. Under such a standard, the gross revenues and affiliations of any investor in the applicant would not be considered so long as the investor holds less than a five percent interest in the applicant. Alternatively, we seek comment on whether we should count the gross revenues of controlling principals in the applicant and its affiliates for purposes of determining small business status. In determining attribution when IVDS licensees are held indirectly through intervening corporate entities, we propose to use the multiplier adopted in the *CMRS Third Report and Order* for the spectrum aggregation cap.<sup>130</sup> We seek comment on these tentative conclusions.

#### **b. Bidding Credits**

71. Background. A bidding credit acts as a discount on the winning bid amount that a bidder actually has to pay for the license. Our current IVDS rules provide for a bidding credit of 25 percent to businesses owned by members of minority groups or women.<sup>131</sup>

72. Discussion. We seek comment on whether we should extend a single bidding credit to all small businesses as we did for the C block PCS auction. If we choose to adopt a single small business bidding credit for IVDS, how big should the credit be? Should we retain the 25 percent bidding credits currently provided and make it available to all small businesses bidding in

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<sup>127</sup> See, e.g., Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, *Second Order on Reconsideration and Seventh Report and Order*, PR Docket No. 89-553, PP Docket No. 93-253, GN Docket No. 93-252, FCC 95-395, 11 FCC Rcd 2639, 60 Fed. Reg. 48913 (Sept. 21, 1995) at ¶ 154, n.320 (*Second Order on Reconsideration and Seventh Report and Order*).

<sup>128</sup> See, e.g., 13 C.F.R. § 121.902.

<sup>129</sup> *Second Order on Reconsideration and Seventh Report and Order*, FCC 95-395, 11 FCC Rcd 2639, 60 Fed. Reg. 48913 (Sept. 21, 1995).

<sup>130</sup> *CMRS Third Report and Order*, 9 FCC Rcd 7988 at ¶ 277; see also *Fifth Memorandum Opinion and Order*, 10 FCC Rcd 403 at ¶ 71, n.169.

<sup>131</sup> 47 C.F.R. § 95.816(d)(1).

the IVDS auction? If we extend a bidding credit to small businesses, we expect that a significant number of women and minority-owned businesses will continue to qualify for bidding credits under our rules.<sup>132</sup> We believe that this may be the most effective way to amend our rules and proceed with the auction. We also believe that this proposal will meet the statutory objectives of promoting economic opportunity and competition, avoiding excessive concentration of licenses, and ensuring access to new and innovative technologies by disseminating licenses among a wide variety of applicants, including small businesses, rural telephone companies, and businesses owned by members of minority groups and women.<sup>133</sup> Moreover, as we observed in the *Fourth Report and Order*, we expect that the capital requirements for IVDS will be relatively low, particularly with respect to the smaller RSA licenses. We therefore anticipate that women- and minority-owned firms, as well as other potential bidders that might lack access to capital, will be able to compete effectively for IVDS licenses. We also point out that the overwhelming majority of IVDS applicants in the past have been small businesses.<sup>134</sup>

73. In the alternative, should we offer tiered bidding credits, such as 15 percent for small businesses with aggregate gross revenues under \$3 million and 10 percent for businesses with gross revenues between \$3 million and \$15 million? We tentatively conclude that, given the relatively low bids that IVDS licenses garnered in the July 1994 auction, IVDS may attract smaller businesses, thus justifying a tiered bidding credit. We seek comments on this tentative conclusion. Commenters are asked to address whether this approach would better reflect the difficulties that small businesses of varying size face in accessing capital. Commenters also should discuss what size definitions and bidding credit amounts are appropriate if the Commission adopts a tiered bidding credit scheme.

74. Commenters are also asked to address whether the Commission should completely eliminate the bidding credit. Commenters should address whether a bidding credit is needed to permit small businesses to compete effectively for IVDS spectrum. As noted above, IVDS, with its relatively low capital entry requirements, is well suited for small business investment and a bidding credit may not be needed to foster participation by these entities.<sup>135</sup> Given the success of small businesses in our MSA auction, commenters are invited to address whether we should revisit that conclusion.

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<sup>132</sup> See, e.g., *Second Report and Order and Second Further Notice of Proposed Rule Making*, PR Docket No. 89-553, 10 FCC Rcd 6884 (1995) ("*900 MHz SMR Second R&O/Second FNPRM*") (indicating that "U.S. Census Data shows that approximately 99% of all women-owned businesses and 99 percent of all minority-owned businesses generated net receipts of \$1 million or less,") citing *Women-Owned Business*, WB87-1, 1987 Economic Census, p. 144, Table 8; *Survey of Minority-Owned Business Enterprises*, MB87-4, 1987 Economic Census, pp. 81-82, Table 8.

<sup>133</sup> See, e.g., *900 MHz SMR Second R&O/Second FNPRM*, 10 FCC Rcd 6884 (1995).

<sup>134</sup> We observe that in the IVDS auction for MSA licenses, 557 of 594 winning bidders (93.8 percent) claimed small business status.

<sup>135</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶¶ 38, 53.

75. While we reluctantly propose to eliminate our race- and gender-based preferences, we conclude that nothing in the *Adarand* decision calls our size-based provisions into question. We note that the Supreme Court held that a strict scrutiny standard of review applies to preferences based on race, not size.<sup>136</sup> Thus, attempts to ensure that small businesses have the opportunity to compete in the provision of IVDS are subject to a less rigorous legal review by the courts. Indeed, our small business installment payment provisions are bolstered by *Adarand* insofar as that decision requires the consideration of race-neutral measures to promote equal opportunity.<sup>137</sup>

## **B. Upfront Payments**

76. Background. In the *Fourth Report and Order*, we determined that the appropriate upfront payment for IVDS auctions would be based on the maximum number of licenses a bidder desired to win.<sup>138</sup> Bidders were required to present a cashier's check for \$2,500 in order to bid on the IVDS licenses, and would be required to have \$2,500 upfront money for every five licenses they won, effectively constituting an upfront payment of \$500 per license won.<sup>139</sup> Following the initial IVDS auction, certain high bidders requested waivers to permit them to delay payment of their required down payments. Further, a substantial number of bidders defaulted on their winning bids, requiring us to reauction those licenses.

77. Discussion. We tentatively conclude that the upfront payment required under the *Fourth Report and Order* is inadequate. In several *ex parte* filings, parties indicated their support for increased upfront payment amounts.<sup>140</sup> The requests for waivers to delay making down payments, coupled with the significant number of defaulting winning bidders, lead us to believe that the initial upfront payment was too low to deter insincere, speculative bidding. We propose that more appropriate upfront payments would be \$9,000 per MSA license and \$2,500 per license for RSA markets, for the maximum number of licenses on which the applicant wishes to bid. We reach these proposed amounts by calculating values for each license of \$.02 per MHz per pop,

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<sup>136</sup> *Adarand*, 115 S.Ct. at 2112-13.

<sup>137</sup> *See id.* at 2118, quoting *Croson*, 488 U.S. at 507 (under strict scrutiny, courts ask "whether there was any consideration of the use of race-neutral means to increase minority business participation.")

<sup>138</sup> 9 FCC Rcd 2330 at ¶ 24.

<sup>139</sup> *Id.*

<sup>140</sup> *See* Letter from Kingdon R. Hughes to Robert H. McNamara, Chief, Private Wireless Division (filed Jan. 25, 1995) at 8-9; Petition for Declaratory Ruling Regarding Bidding Credit and Informal Request for Adjustment in Price filed by Hardiner Kumra (filed Oct. 19, 1994) at 3-6; Informal Request for Adjustment of Auction Price filed by IGGW Interactive, Inc. (filed Oct. 19, 1995) at 3-6; and Petition for Special and Extraordinary Relief filed by MKS Interactive, Inc. (filed Nov. 1, 1994) at 5, 13.



which is the standard methodology for determining upfront payment amounts.<sup>141</sup> This calculation yielded average upfront payments of approximately \$9,011 per license for MSA markets (not counting the 9 markets previously awarded by lottery), and approximately \$2,742 per license for RSA markets. Our proposed upfront payments round these figures. We believe that revised upfront payments in these amounts would attract as many qualified bidders as possible, while providing an adequate deterrent against frivolous bidding. We seek comment on our tentative conclusion and our proposal to increase the upfront payment amounts as described.

## VI. PROCEDURAL MATTERS

78. Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. § 604, the Commission's final analysis for the *Sixth Memorandum Opinion and Order and Further Notice of Proposed Rule Making* is as follows:

79. Need for and purpose of this action. As a result of new statutory authority, the Commission may utilize competitive bidding mechanisms in the granting of certain initial licenses. The Commission published an Initial Regulatory Flexibility Analysis, *see generally* 5 U.S.C. § 603, within the *Notice of Proposed Rule Making* in this proceeding (at 8 FCC Rcd 7635, Appendix at 7666 (1993)), and published Final Regulatory Flexibility Analyses within the *Second Report and Order* (at 2400 ¶¶ 299-302) and the *Fourth Report and Order* (at 2340-41 ¶ 56). As noted in these previous final analyses, this proceeding will establish a system of competitive bidding for choosing among certain applications for initial licenses, and will carry out statutory mandates that certain designated entities, including small entities, be afforded an opportunity to participate in the competitive bidding process and in the provision of spectrum-based services.

80. Summary of the issues raised by the public comments in response to the Initial Regulatory Flexibility Analysis. As this is an Order on Reconsideration, there is no initial regulatory flexibility analysis to which petitioners are responding. There were no petitions which discussed the final regulatory flexibility analysis in the underlying order.

81. Significant alternatives considered. Although no comments were received pertaining to the IVDS, the *Second Report and Order* and *Fourth Report and Order* addressed at length the general policy considerations raised as a result of the Commission's new auction authority.

82. With respect to the *Memorandum Opinion and Order* reconsidering our rules, a Final Regulatory Flexibility Analysis (FRFA), in compliance with 5 U.S.C. Section 801, is contained in

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<sup>141</sup> With the "MHz-pop" methodology, "pop" refers to each member of the population of the license service area, and "MHz" refers to the amount of spectrum, in megahertz, that the licensee is permitted to use. *See Second Report and Order* at 2378 ¶ 172, 2379 ¶ 180; *Notice of Proposed Rule Making* in PP Docket No. 93-253, 8 FCC Rcd 7635, 7652 n. 98 (1993). *See also Fourth Report and Order*, 9 FCC Rcd 2330, 2334 n.41.

Appendix B. Also, with respect to the *Further Notice of Proposed Rule Making* an Initial Regulatory Flexibility Analysis is contained in Appendix B. As required by Section 603 of the Regulatory Flexibility Act, the Commission has prepared an Initial Regulatory Flexibility Analysis (IRFA) of the expected impact on small entities of the proposals suggested in this document. Written public comments are requested on the IRFA. These comments must be filed in accordance with the same filing deadlines as comments on the rest of the Further Notice of Proposed Rule Making, but they must have a separate and distinct heading designating them as responses to the Initial Regulatory Flexibility Analysis. The Secretary shall send a copy of this Further Notice of Proposed Rule Making, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act. Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. § 601 *et seq.* (1981).

83. This is a non-restricted notice and comment rule making proceeding. *Ex parte* presentations are permitted except during the Sunshine Agenda period, provided they are disclosed as provided in Commission rules. *See generally* 47 C.F.R. §§ 1.1202, 1.1203, and 1.1206(a).

84. Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules, 47 C.F.R. §§ 1.415 and 1.419, interested parties may file comments on or before 15 days from publication of notice in the Federal Register and reply comments on or before 7 days from the deadline for comments. To file formally in this proceeding you must file an original and four copies of all comments and supporting comments. If you want each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. You should send your comments to Office of the Secretary, Federal Communications Commission, 1919 M Street, N.W., Washington, D.C. 20554. Comments will be available for public inspection during regular business hours in the Reference Center of the Federal Communications Commission, 1919 M Street, N.W., Room 239, Washington, D.C. 20554.

85. Authority for issuance of this *Sixth Memorandum Opinion and Order and Further Notice of Proposed Rule Making* is contained in Sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 303(r) and 309(j).

86. Accordingly, IT IS ORDERED that, pursuant to the authority of Sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 303(r), and 309(j), this *Sixth Memorandum Opinion and Order* is adopted, and Parts 1 and 95 of the Commission's Rules ARE AMENDED as set forth in Appendix A.

87. IT IS FURTHER ORDERED that the rule changes made herein WILL BECOME EFFECTIVE 60 days after their publication in the Federal Register. IT IS FURTHER ORDERED that, as described above, the petition for reconsideration filed by ITV IS GRANTED in part to the extent described above and IS DENIED in all other respects, the petitions for reconsideration filed by Phase One, RCA, and USIN ARE DENIED, and the petition for rule

making filed by ITA IS DENIED.

88. For further information concerning this proceeding, contact Christina Eads Clearwater at (202) 418-0660 (Auctions Division, Wireless Telecommunications Bureau).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton  
Acting Secretary

## APPENDIX A

### FINAL RULES

Parts 1 and 95 of Chapter 1 of Title 47 of the Code of Federal Regulations are amended as follows:

#### **Part 1 - Practice and Procedure**

1. Section 1.2107 is amended by revising paragraph (c) to read as follows:

##### **§ 1.2107 Submission of down payment and filing of long-form applications.**

\* \* \* \* \*

(c) A high bidder that meets its down payment obligations in a timely manner must, within ten (10) business days after being notified that it is a high bidder, submit an additional application (the "long-form application") pursuant to the rules governing the service in which the applicant is the high bidder (unless it has already submitted such an application, as contemplated by Sec. 1.2105(a)(1)(b)). For example, if the applicant is high bidder for a license in the Interactive Video Data Service (see 47 C.F.R. Part 95, Subpart F), the long form application will be submitted on FCC Form 600 in accordance with Sec. 95.815 of this chapter. Notwithstanding any other provision in title 47 of the Code of Federal Regulations to the contrary, high bidders need not submit an additional application filing fee with their long-form applications. Notwithstanding any other provision in Title 47 of the Code of Federal Regulations to the contrary, the high bidder's long-form application must be mailed or otherwise delivered to: Office of the Secretary, Federal Communications Commission, Attention: Auction Application Processing Section, 1919 M Street, N.W., Room 222, Washington, D.C. 20554. An applicant that fails to submit the required long-form application as required under this subsection, and fails to establish good cause for any late-filed submission, shall be deemed to have defaulted and will be subject to the penalties set forth in Sec. 1.2104.

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#### **Part 95 - Personal Radio Services**

2. Section 95.815 is amended by revising paragraphs (b), (d)(2), and (f)(3) to read as follows:

##### **§ 95.815 License Application.**

\* \* \* \* \*

(b) Each application for an IVDS system license must be made on a separate FCC Form 600, and must be submitted to the Federal Communications Commission, Interactive Video and Data Service, P.O. Box 358365, Pittsburgh, PA 15251-5365. Each application for a CTS license

where the CTS antenna exceeds 6.1m (20 feet) (see § 95.811(b)) must be made on a separate FCC Form 574, and must be submitted to the address set forth in § 1.1102 of the Commission's Rules.

\* \* \* \* \*

(d) \* \* \*

(2) A completed application (FCC Form 600).

\* \* \* \* \*

(f) \* \* \*

(3) A separate application (FCC Form 600) for each CTS that is being added or modified.

\* \* \* \* \*

3. Section 95.816 is amended by revising paragraphs (c)(1), (c)(2), (c)(4), (c)(6), and (d)(1); deleting paragraph (d)(2); and revising paragraph (d)(3) and redesignating it as (d)(2); and adding a new paragraph (d)(3). The amended Section 95.816 reads as follows:

**§ 95.816 Competitive bidding proceedings.**

\* \* \* \* \*

(c) \* \* \*

(1) Competitive bidding design options and mechanisms. The Wireless Telecommunications Bureau will select competitive bidding design(s) and mechanisms in accordance with Sections 1.2103 and 1.2104 of this Chapter. If simultaneous multiple round bidding is used, the Wireless Telecommunications Bureau has the discretion to vary the duration of the bidding rounds or the interval at which bids are accepted at any time before or during the course of the auction.

(2) Forms.

(i) Applicants must submit short-form applications (FCC Form 175) as specified in Commission Public Notices. Minor deficiencies may be corrected prior to the auction. Major modifications such as changes in ownership, failure to sign an application or failure to submit required certifications will result in the dismissal of the application. *See* §§ 1.2105(a) and (b) of this Chapter.

(ii) Applicants must submit a long-form application (FCC Form 600) within ten (10) business days after being notified that it is the winning bidder for a license. *See* §§ 1.2107(c) and (d) of this Chapter.

\* \* \* \* \*

(4) Down payments. *See* § 1.2107(b) of this Chapter.

\* \* \* \* \*

(6) Withdrawal, default or disqualification. *See* §§ 1.2104(g) and 1.2109 of this Chapter.

\* \* \* \* \*

(d) \* \* \*

(1) Bidding credits. A winning bidder that qualifies as a business owned by women and/or minorities may use a bidding credit of twenty five (25) percent to lower the cost of its winning bid.

(2) Installment payments. Each licensee that qualifies as a small business may pay the remaining 80 percent of the net auction price in quarterly installment payments pursuant to § 1.2110(e) of this Chapter. Licensees who qualify for installment payments are entitled to pay their winning bid amount in installments over the term of the license, with interest charges to be fixed at the time of licensing at a rate equal to the rate for five-year U.S. Treasury obligations. Payments shall include interest only for the first two years and payments of interest and principal amortized over the remaining three years of the license term. A license issued to an eligible small business that elects installment payments shall be conditioned on the full and timely performance of the license holder's quarterly payments.

(3) Audits.

(i) Applicants and licensees claiming eligibility under this section shall be subject to audits by the Commission, using in-house and contract resources. Selection for audit may be random, on information, or on the basis of other factors.

(ii) Consent to such audits is part of the certification included in the short-form application (Form 175). Such consent shall include consent to the audit of the applicant's or licensee's books, documents, and other material (including accounting procedures and practices) regardless of form or type, sufficient to confirm that such applicant's or licensee's representations are, and remain, accurate. Such consent shall include inspection at all reasonable times of the facilities, or parts thereof, engaged in providing and transacting business, or keeping records regarding licensed IVDS and shall also include consent to the interview of principals, employees, customers and suppliers of the applicant or licensee.

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## APPENDIX B

### I. Final Regulatory Flexibility Analysis

#### *Sixth Memorandum Opinion and Order*

This action reconsiders rules previously adopted by the Commission and is authorized under Section 405 of the Communications Act, 47 U.S.C. § 405. Because the action is not generated by a Notice of Proposed Rule Making, there is no applicable Initial Regulatory Flexibility Act analysis to which it responds. However, the Commission's Final Regulatory Flexibility Analysis (FRFA) in this Order conforms to the RFA, as amended by the Contract with America Advancement Act of 1996 (CWAAA), Pub. L. No. 104-131, 110 Stat. 847 (1996).<sup>142</sup>

#### A. Need for and Objective of the Rules

This Order adopts rule changes regarding the Commission's auction of Interactive Video and Data Service (IVDS) licenses. The rule changes are appropriate because: (1) laws have changed since the rules were originally adopted; namely, the tax certificate program which encouraged investment in minority- and women-owned IVDS bidders, was eliminated; (2) the Supreme Court's decision in *Adarand Constructors, Inc. v. Peña* 115 S. Ct. 2097 (1995), raised the level of legal scrutiny that must be met by some of the designated entity programs which take race into account; and (3) petitions for reconsideration of our earlier orders have caused us to review the rules in a new light. The objective of the Order is to bring the benefit of our experience from the first IVDS auction to subsequent IVDS auctions, and to make opportunities available to small businesses to operate in the service. The most significant changes being made are: to allow IVDS licenses to be auctioned using a simultaneous multiple round auction methodology; to eliminate the tax certificate program for licensees; and to extend bidding credits to both licenses in each IVDS market.

#### B. Summary of Issues Raised by Public Comment on the Initial Regulatory Flexibility Analysis

As this is an Order on Reconsideration, there is no initial regulatory flexibility analysis to which petitioners are responding. There were no petitions which discussed the final regulatory flexibility analysis in the underlying order.

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<sup>142</sup> Subtitle II of the CWAAA is "The Small Business Regulatory Enforcement Fairness Act of 1996" (SBREFA), codified at 5 U.S.C. § 601, *et. seq.*

### **C. Projected Reporting, Recordkeeping and Other Compliance Requirements of the Rules**

#### *Authorizing use of simultaneous multiple round auctions*

The Commission, on its own motion, is adopting a rule which will permit IVDS licenses to be auctioned using a simultaneous multiple round auction in addition to oral outcry auctions. The Commission is recommending the use of an oral outcry auction for the RSA and re-auctioned licenses, but it is trying to add flexibility in the event that a simultaneous multiple round auction would be more appropriate at some later point. A simultaneous multiple round auction will allow remote access to bidding software, auction information, bid submission and results. This will make it easier for small business operators to participate in an auction without leaving their places of business. Also, it will make information concerning the status of the auction easier to access, which will reduce the administrative burden on participants in the auction. There are no other reporting, recordkeeping or compliance changes which would result from this rule change.

#### *Elimination of the Tax Certificate Program*

The Commission had authority under Title 26 of the United States Code, 26 U.S.C. § 1071, to issue tax certificates to benefit women and/or minority owned businesses. In 1995, Congress repealed Section 1071. This rule is being eliminated to comply with the tax code.

#### *Bidding Credits Extended to Both Licenses in Each MSA*

The Commission originally wrote its rules to permit a bidding credit to be awarded to only one auction winner in each MSA. Originally, a minority- or woman-owned business designated entity auction winner who did not receive a bidding credit was free to transfer its license and gain the benefits of a tax certificate. The auction winner who received a bidding credit was subject to unjust enrichment penalties if it transferred the license. The tax certificate acted as the equivalent of a bidding credit, helping an auction winner attract capital. If the auction winner's license was transferred to a designated entity, or the winner is a designated entity, the tax certificate would provide a financial incentive for transacting business with the designated entity. In the absence of a tax certificate program, small businesses with gross revenues under the requisite levels will be eligible for a bidding credit on both licenses in the MSA. The companies eligible for these bidding credits will have to provide information to the Commission which establishes that they meet the qualifications to receive the bidding credit. This reporting requirement is necessary to avoid fraud on the public.

#### *Long Form Application Changed to Form 600*

Applicants were required to submit financial information regarding their qualification to hold a license on an FCC Form 574. The Commission has secured approval by the Office of



Management and Budget for the use of the FCC Form 600.<sup>143</sup> This form collects more accurate and complete financial information regarding applicants than the form used in the first IVDS auction. As a result, it helps the Commission ensure that the applicants for licenses are fully qualified to hold licenses, reducing the amount of time that radio spectrum would sit unused, if it were subject to legal dispute.

#### *Winning Bidders May Receive Upfront Payment Refund*

One petitioner, ITV, Inc., requested that, when upfront money on deposit exceeded the amount necessary for a winning bidder to make its down payment, the excess funds be refunded to the bidder. *See supra* ¶¶ 32-34. We granted the request to change our rules to alleviate one source of financial constraint on small businesses. This will not result in any changed reporting or recordkeeping. It could reduce the need to secure additional interim financing.

All of these changes were made to encourage the participation of designated entities in the auctions of IVDS licenses, as section 309(j) of the Communications Act requires.

#### **D. Description and Estimate of Small Entities Subject to the Rules**

The proposed changes in the regulations would affect a number of entities both large and small. The Commission was directed by the Communications Act, 47 U.S.C. § 309(j) to make provisions to ensure that smaller businesses, and other designated entities, have an opportunity to participate in the auction process. To fulfill this statutory mandate, these proposed rules are designed to attract participation by small entities. The small businesses who will be subject to the rules would be those which choose to operate interactive video and data services, a class of wireless communications services with a wide variety of uses. The services will generally be offered to consumers who wish to subscribe to those services.

IVDS is a communications-based service subject to regulation as a wireless provider of pay television services under Standard Industrial Classification 4841 (SIC 4841), which covers subscription television services.<sup>144</sup> The Small Business Administration (SBA) defines small businesses in SIC 4841 as businesses with annual gross revenues of \$11 million or less. 13 C.F.R. § 121.201. In this *Further Notice*, we propose to extend special provisions to small businesses with annual gross revenues of \$15 million or less and additional benefits to very small businesses with annual gross revenues of \$3 million or less. We observe that this proposal is consistent with

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<sup>143</sup> *See* Notice of Public Information Collections Submitted to OMB for Review and Approval, 61 Fed. Reg. 3699 (Feb. 1, 1996).

<sup>144</sup> Generally, IVDS services will be subscriber-based services providing video communications which could be described as a form of subscription television service.

our approach in other wireless services, *see e.g.*, the 900 MHz specialized mobile radio service, and is narrowly tailored to address the capital requirements for IVDS. The Commission is soliciting SBA approval for the small business definitions for this and other auctionable services.

The Commission's estimate of the number of small business entities subject to the rules begins with the Bureau of Census report on businesses listed under SIC 4841, subscription television services. The total number of entities under this category is 1,788.<sup>145</sup> There are 1,463 companies in the 1992 Census Bureau report which are categorized as small businesses providing cable and pay TV services.<sup>146</sup> We know that many of these businesses are cable and television service businesses, rather than IVDS licensees. Therefore, the number of small entities currently in this business which will be subject to the rules will be less than 1,463.

The first IVDS auction resulted in 170 entities winning licenses for 594 MSA licenses. Of the 594 licenses, 557 were won by entities qualifying as a small business. For that auction, we defined a small business as an entity, together with its affiliates, that has no more than a \$6 million net worth and, after Federal income taxes (excluding any carry over losses), has no more than \$2 million in annual profits each year for the previous two years.<sup>147</sup> In the upcoming IVDS re-auction of approximately 100 licenses in metropolitan service area (MSA) markets and auction of 856 licenses in rural service area (RSA) markets (two licenses per market), we have proposed bidding credits and installment payments to encourage participation by small and very small businesses. We cannot estimate, however, the number of licenses that will be won by entities qualifying as small or very small businesses under our proposed rules. Given the success of small businesses in past IVDS auctions, and that small businesses make up over 80 percent of firms in the subscription television services industry, we assume for purposes of this IRFA that all of the licenses may be awarded to small businesses, which would be affected by the rules we propose. We estimate that some companies will win more than one license, as happened in the earlier IVDS auction.

Applicants seeking to participate in the auction also will be subject to these proposed rules. It is impossible to accurately predict how many small businesses will apply to participate in the auction. In the last IVDS auction, there were 289 qualified applicants. We do not anticipate

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<sup>145</sup> U.S. Small Business Administration 1992 Economic Census Industry and Enterprise Report, Table 2D, SIC Code 4841 (Bureau of the Census data adapted by the Office of Advocacy of the U.S. Small Business Administration).

<sup>146</sup> The Census table divides those companies by the amount of annual receipts. There is a dividing point at companies with annual receipts of \$10 million. The next increment is annual receipts of \$17 million, a category that greatly exceeds the SBA definition of small businesses that provide subscription television services. However, there are 17 firms in this category, with revenues between \$10-\$17 million. Approximately 1,480 SIC 4841 category firms have annual gross receipts of \$15 million or less. Only a small fraction of those 1,480 firms provide interactive video and data services.

<sup>147</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 36.

that there will be significantly more participants in the subsequent IVDS auction.

#### **E. Steps Taken to Minimize the Burdens on Small Entities**

The changes made in the *Sixth Memorandum Opinion and Order* are designed to minimize burdens on small businesses. The extension of an additional bidding credit to the second license in each market will assist businesses owned by women and minorities. Most of the businesses owned by women and minorities which have participated in the FCC's auctions are small businesses which will benefit from this rule. This rule change will benefit small businesses owned by women and minorities by doubling the number of bidding credits available to them.

Refunds of excess upfront payments on deposit will benefit small businesses. Smaller businesses often have more difficulty raising capital. The rules permitted the retention of any excess upfront payments on deposit with the FCC to apply to down payments or to bid withdrawal payments. 47 C.F.R. §1.2106. While an upfront payment is an important part of ensuring that only serious bidders participate in the Commission's auction process, it is also important that small businesses have an opportunity to put their more limited funds to the best possible use. By assuring the return of excess funds after the first down payment and any withdrawal penalties are paid, small businesses will have those funds to use as they wish.

By adding an auction methodology, the Commission adds flexibility to its auction process. One advantage of simultaneous multiple round auctions is that they can make it possible for bidders to participate from their own places of business. That is an advantage under some auction circumstances. The Commission has chosen to use an oral outcry auction for the RSA license auction, and for the first MSA licenses which will be re-auctioned, because an oral outcry auction will be most efficient. *See supra* Paragraphs 15-16.

#### **F. Significant Alternatives Considered and Rejected**

##### *Authorizing use of simultaneous multiple round auctions*

We do not currently have plans to use a simultaneous multiple round auction for this service. The rule is being added should it become necessary at a later time to re-auction licenses which have developed a higher degree of interdependence. Because this rule adds administrative expediency, which will speed the issuance of licenses, we have chosen to add the option of an additional auction methodology for this service. The Commission is acting to minimize delays in the close of an auction by adding flexibility to its stopping and activity rules. We determined that the alternative of leaving the rules unchanged could delay the auction process at some time in the future.

##### *Elimination of the Tax Certificate Program*

All small businesses owned by members of minority groups or women who choose to participate in the auction for IVDS licenses will be subject to this rule change. Due to the repeal of the tax code provision, the Commission has no choice but to eliminate this provision which benefitted these small businesses.

#### *Bidding Credits Extended on Both Licenses in Each MSA*

This rule will apply to any small businesses owned by women or minorities that are eligible for bidding credits which participate in the re-auction of MSA licenses.<sup>148</sup> We considered leaving the rules unchanged, but, in the absence of the tax certificate program, the rules may have unfairly disadvantaged some minority or women owned small businesses while offering greater advantages to some of their competitors. Therefore, in eliminating the tax certificate program, we felt it was necessary to extend the bidding credit to both licenses in each market. The Commission considered the extension of bidding credits to rural telephone companies.<sup>149</sup> The Commission offers bidding credits to businesses owned by women or minorities to provide an incentive for those businesses to enter the communications industry. Rural telephone companies are already participants in this industry. The Commission was not required to make all benefits available to all designated entities. Consequently, in weighing the competing public policy concerns with respect to bidding credits, the Commission chose not to extend bidding credits to rural telephone companies.

#### *Long Form Application Changed to Form 600*

This rule will enable the Commission to more effectively evaluate applications filed for IVDS licenses. The Commission did not consider alternatives because, in adapting its processes to auctions, the Commission has concentrated on reducing the number of different forms and steps that auction participants will have to master to participate in the process. Because all other auctionable services have shifted to the Form 600, IVDS auction participants will be able to use information they may have filed for other auctionable services in any future IVDS auctions as well.

#### *Winning Bidders May Receive Upfront Payment Refund*

The rules previously did not make clear that an auction winner could receive a refund of any excess monies on deposit with the FCC, after payment of the first down payment and any penalties due. This rule change was made to ensure that businesses which win IVDS licenses have as much capital available to build systems and serve the public as possible. Because the rule change results in returning money to businesses, the Commission did not consider alternatives in making this change.

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<sup>148</sup> This rule is proposed to be changed in the accompanying *Further Notice of Proposed Rule Making*.

<sup>149</sup> See e.g., Petition for Reconsideration of Rural Cellular Association (filed June 13, 1994).

**G. Commission's Outreach Efforts to Learn of and Respond to the Views of Small Entities Pursuant to 5 U.S.C. § 609**

The Commission did not seek specific comments regarding small entities' views of the rules being changed because the petitions and comments were filed in this proceeding prior to the enactment of the 1996 Regulatory Flexibility Act Amendments. However, the Commission, in making changes to the rules, has sought to alleviate burdens on small businesses. When Congress authorized the FCC to use auctions, it instructed the FCC to make provisions for designated entities, including small businesses, when it designed competitive bidding mechanisms.

**H. Report to Congress**

The Commission shall send a copy of this Final Regulatory Flexibility Analysis, along with this *Memorandum Opinion and Order* in a report to Congress pursuant to the Small Business Regulatory Enforcement Fairness Act of 1996, 4 U.S.C. § 801(a)(1)(A). A copy of this Final Regulatory Flexibility Analysis will also be published in the Federal Register.

**II. Initial Regulatory Flexibility Analysis**

***Further Notice of Proposed Rulemaking***

As required by Section 603 of the Regulatory Flexibility Act, the Commission has prepared an Initial Regulatory Flexibility Analysis (IRFA) of the expected impact on small entities of the policies and rules proposed in this *Further Notice of Proposed Rule Making* regarding the interactive video and data service (IVDS). Written public comments are requested on the IRFA. Comments must have a separate and distinct heading designating them as responses to the IRFA and must be filed by the comment deadlines provided above.

**A. Reason for Action:**

The further notice in this rule making proceeding was initiated to secure comment on proposals to eliminate all race- and gender-based provisions in our competitive bidding rules for the IVDS auction only. The proposals advanced in the *Further Notice of Proposed Rule Making* also are designed to implement Congress's goal of giving small businesses, rural telephone companies, and businesses owned by members of minority groups and women the opportunity to participate in the provision of spectrum-based services in accordance with 47 U.S.C. § 309(j)(4)(D). The Commission also seeks to modify its rule concerning the amount it requires for upfront payments from applicants to participate in the auction in accordance with 47 U.S.C. § 309(j)(3).

## **B. Objectives:**

The Commission proposes changes to its rules for IVDS to address legal uncertainties raised by the Supreme Court's decision in *Adarand Constructors, Inc. v. Peña* 115 S.Ct. 2097 (1995). Specifically, the Commission seeks to ensure competition and ownership diversity by avoiding a lengthy delay in conducting the auction caused by possible legal challenges to our rules, which provided bidding credits and other provisions to minority- and women-owned businesses. The Commission proposes to base the provision of bidding credits on the size of the business, rather than on the race or gender affiliation of the owner(s). The Commission also proposes to increase the upfront payment amounts for IVDS licenses because: it believes the current upfront payment amount was insufficient to ensure against a significant number of defaulting winning bidders; and to ensure payment of applicable penalties arising from defaults.

## **C. Legal Basis:**

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

## **D. Description and Estimate of Small Entities Subject to the Rules:**

The proposed changes in the regulations would affect a number of entities both large and small. The Commission was directed by the Communications Act, 47 U.S.C. § 309(j) to make provisions to ensure that small businesses, and other designated entities, have an opportunity to participate in the provision of spectrum based services. To fulfill this statutory mandate, these proposed rules are designed to attract participation by the small entities. The small businesses who will be subject to the rules would be those which choose to operate interactive video and data services, a class of wireless communications services with a wide variety of uses. The services will generally be offered to consumers who wish to subscribe to those services.

IVDS is a communications-based service subject to regulation as a wireless provider of pay television services under Standard Industrial Classification 4841 (SIC 4841), which covers subscription television services.<sup>150</sup> The Small Business Administration (SBA) defines small businesses in SIC 4841 as businesses with annual gross revenues of \$11 million or less. 13 C.F.R. § 121.201. In this *Further Notice*, we propose to extend special provisions to small businesses with average gross revenues for each of the preceding three (3) years that do not exceed \$15 million, and additional benefits to very small businesses who have less than an average of \$3 million in gross revenues in each of the last three years. *See supra* ¶ 69. We observe that this proposal is consistent with our

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<sup>150</sup> Generally, IVDS services will be subscriber-based services providing video communications which could be described as a form of subscription television service.

approach in other wireless services, *see e.g.*, the 900 MHz specialized mobile radio service, and is narrowly tailored to address the capital requirements for IVDS. The Commission is soliciting SBA approval for the small business definitions for this and other auctionable services.

The Commission estimate of the number of small business entities subject to the rules begins with the Bureau of Census report on businesses listed under SIC 4841, subscription television services. The total number of entities under this category is 1,788.<sup>151</sup> There are 1,463 companies in the 1992 Census Bureau report which are categorized as small businesses providing cable and pay TV services.<sup>152</sup> We know that many of these businesses are cable and television service businesses, rather than IVDS licensees. Therefore, the number of small entities currently in this business which will be subject to the rules will be less than 1,463.

The first IVDS auction resulted in 170 entities winning licenses for 594 MSA licenses. Of the 594 licenses, 557 were won by entities qualifying as a small business. For that auction, we defined a small business as an entity with a net worth not in excess of \$6 million and average net income after Federal income taxes for the two preceding years not in excess of \$2 million.<sup>153</sup> In the upcoming IVDS re-auction of approximately 100 licenses in metropolitan service area (MSA) markets and auction of 856 licenses in rural service area (RSA) markets (two licenses per market), we have proposed bidding credits and installment payments to encourage participation by small and very small businesses. We cannot estimate, however, the number of licenses that will be won by entities qualifying as small or very small businesses under our proposed rules. Given the success of small businesses in past IVDS auctions, and that small businesses make up over 80 percent of firms in the subscription television services industry, we assume for purposes of this IRFA that all of the licenses may be awarded to small businesses, which would be affected by the rules we propose. We estimate that some companies will win more than one license, as happened in the earlier IVDS auction.

Applicants seeking to participate in the auction also will be subject to these proposed rules. It is impossible to accurately predict how many small businesses will apply to participate in the auction. In the last IVDS auction, there were 289 qualified applicants. We do not anticipate that there will be significantly more participants in the subsequent IVDS auction.

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<sup>151</sup> U.S. Small Business Administration 1992 Economic Census Industry and Enterprise Report, Table 2D, SIC Code 4841 (Bureau of the Census data adapted by the Office of Advocacy of the U.S. Small Business Administration).

<sup>152</sup> The Census table divides those companies by the amount of annual receipts. There is a dividing point at companies with annual receipts of \$10 million. The next increment is annual receipts of \$17 million, a category that greatly exceeds the SBA definition of small businesses that provide subscription television services. However, there are 17 firms in this category, with revenues between \$10-\$17 million. Approximately 1,480 SIC 4841 category firms have annual gross receipts of \$15 million or less. Only a small fraction of those 1,480 firms provide interactive video and data services.

<sup>153</sup> *Fourth Report and Order*, 9 FCC Rcd 2330 at ¶ 36.

**E. Reporting, Recordkeeping and Other Compliance Requirements:**

All small businesses which choose to participate in these services will be required to demonstrate that they meet the criteria set forth to qualify as small businesses, as was required under part 1, subpart Q of the FCC's Rules, 47 C.F.R. part 1, subpart Q. Any small business applicant wishing to avail itself of those provisions will need to make the general financial disclosures necessary to establish that the small business is in fact small. The proposed rule changes will eliminate the requirements that small businesses owned by minorities and/or women demonstrate that their owners are minorities and/or women. There are no additional reporting or recordkeeping requirements proposed by these rules.

Each small business applicant will be required to submit an FCC Form 175, OMB Clearance Number 3060-0600. The estimated time for filling out an FCC Form 175 is 45 minutes. In addition to filing an FCC Form 175, each applicant must submit information regarding the ownership of the applicant, any joint venture arrangements or bidding consortia that the applicant has entered into, and financial information which demonstrates that a small business wishing to qualify for installment payments and bidding credits is a small business. Applicants which do not have audited financial statements available will be permitted to certify to the validity of their financial showings. While many small businesses have chosen to employ attorneys prior to filing an application to participate in an auction, the rules are proposed so that a small business working with the information in a bidder information package can file an application on its own. When an applicant wins a license, it will be required to submit an FCC Form 600, *see supra* ¶ 50, which will require technical information regarding the applicant's proposals for providing service. This application will require information provided by an engineer who will have knowledge of the system's design.

**F. Federal Rules Which May Overlap, Duplicate or Conflict With These Rules:**

None.

**G. Significant Alternative Minimizing the Impact on Small Entities Consistent with the Stated Objectives:**

In the *Further Notice of Proposed Rule Making*, the Commission tentatively concludes that the possibility of legal challenges to the rules could cause lengthy delays in issuing licenses in this service. Since the first IVDS auction, the Supreme Court in *Adarand v. Peña*, 115 S. Ct. 2097 (1995) raised the legal standard for assessing the constitutionality of federal programs which take race into account. Such programs are now subject to a strict scrutiny standard of review. Although programs which take gender into account are reviewed under an intermediate scrutiny standard of review, *United States v. Commonwealth of Virginia* 1996 WL 345786 (United States Supreme Court, June 26, 1996) (*VMI*), we believe there is a significant risk, under either standard, that the auction would be subject to delay through litigation over the constitutionality of the program. The



Commission is currently gathering evidence, through a Notice of Inquiry proceeding pursuant to Section 257 of the Telecommunications Act of 1996, on barriers to market entry for small businesses, including those owned by women and minorities.<sup>154</sup> We realize that this change may impose a burden on small businesses owned by women or minorities.<sup>155</sup> We seek comment on whether there are alternatives which will enable us to avoid litigation delays, which adversely affect all small businesses, and still make provision for these designated entities.

The *Further Notice of Proposed Rule Making* solicits comment on a variety of alternatives set forth herein. Any significant alternatives presented in the comments will be considered. The *Further Notice of Proposed Rule Making* proposes setting new standards for the measurement of small businesses. The earlier standard defined a small business as an entity, together with its affiliates, that has no more than a \$6 million net worth and, after federal income taxes (excluding any carry over losses), has no more than \$2 million in annual profits each year for the previous two years. 47 C.F.R. § 1.2110. We are proposing to define a small business as a business with average gross revenues for each of the preceding three (3) years that do not exceed \$15 million, and define a very small business as one which has less than an average of \$3 million in gross revenues in each of the last three years. *See supra* ¶ 69. We seek comment on the classes of small entities and how many total entities, existing and potential, would be affected by the proposed rules in the *Further Notice of Proposed Rule Making*. These changes would be consistent with the definitions used in other auctionable mobile radio services such as 900 MHz specialized mobile radio services.<sup>156</sup> We request each commenter to identify whether it is a "small business" under this definition.

The *Further Notice of Proposed Rule Making* proposes providing a bidding credit to small businesses. The Commission seeks comment on whether a 25 percent bidding credit is appropriate for all small businesses or whether a tiered bidding credit, 10 percent for small businesses and 15 percent for very small businesses, is appropriate. We seek comment on the impact of the creation of a larger pool of small businesses eligible for bidding credits. We propose businesses with average gross revenues of \$15 million or less in each of the last three (3) years be eligible for bidding credits, as opposed to the previous standard of an entity, together with its affiliates, that has no more than a \$6 million net worth and, after federal income taxes (excluding any carry over losses), has no more than \$2 million in annual profits each year for the previous two years. We request comment on how this larger pool of small businesses will affect the smaller businesses which choose to participate in

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<sup>154</sup> In the Matter of Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Businesses, Notice of Inquiry, GN Dkt. No. 96-113, FCC 96-216 (adopted May 10, 1996, released May 21, 1996), 11 FCC Rcd 6281 (1996).

<sup>155</sup> Of the 594 IVDS licenses auctioned initially, 140 were won by bidders claiming minority-owned status, 227 were won by bidders claiming woman-owned status, and 55 were won by bidders claiming minority and woman-owned status. FCC's 1994 Visitor's Auction Guide, released December 5, 1994.

<sup>156</sup> *See supra*, Paragraph 69. *See also Second Order on Reconsideration and Seventh Report and Order*, FCC 95-395, 60 Fed. Reg. 48913 (Sept 21, 1995).

the auction. Additionally, we are particularly interested in learning whether tiered bidding credits will offset any potential competitive disadvantage to those smaller businesses.

The Commission proposes to raise the upfront payment to \$9,000 per MSA and \$2,500 per RSA for businesses participating in IVDS auctions. This rule change is designed minimize the adverse impact on the IVDS service of participation in the auction by speculators and other frivolous bidders. The Commission realizes that a higher upfront payment may pose a greater obstacle to participation by smaller businesses. We seek comment on our tentative conclusion that the previous upfront payment was too low. We also request commenters to address the question of whether there are other means to deter speculative or frivolous bidders who do not meet the commitments they make in bidding in IVDS auctions.

## **APPENDIX C**

### **LIST OF PARTIES**

#### **Petitions for Reconsideration**

ITV, Inc.  
Phase One Communications, Inc.  
Rural Cellular Association  
U.S. Intelco Networks, Inc.

#### **Comments**

Quentin L. Breen  
U.S. Telephone Association

#### **Petition for Rule Making**

Interactive Television Association

#### **Comments**

Cyrus K. Dam  
George C. Dick  
John D. Elliott