alienability restrictions - it cannot be sold, pledged, mortgaged, or otherwise encumbered.[98] Thus, Native corporations are precluded from two of the most important means of raising capital enjoyed by virtually every other corporation: (1) the ability to pledge stock of the company against ordinary borrowings, and (2) the ability to issue new stock or debt securities.[99] In addition, assets held by Indian tribes include land holdings that cannot be used as collateral for purposes of raising capital, because the land holdings are owned in trust by the federal government or are subject to a restraint on alienation in the government's favor.[100] Congress has not placed similar legal constraints on the assets and revenues of enterprises owned by any other minority group. We agree with Cook Inlet that such legal restraints on assets and revenues place Indian tribes at a disadvantage vis-a-vis other minority groups with similar revenues and assets.[101] Finally, as we noted in our *Order on Reconsideration*, Congress has mandated that the SBA determine the size of a business concern owned by a tribe without regard to the concern's affiliation with the Indian tribe.[102] Our policy mirrors this congressional mandate.

44. After considering the record, however, we have determined that gaming revenues generally are not subject to the same types of legal restrictions as other revenues received by Indian tribes.[103] Therefore, we establish a rebuttable presumption that revenues derived from gaming pursuant to the Indian Gaming Regulatory Act, 25 U.S.C. § 2701 *et seq.*, will be included in our calculations when determining whether an applicant that is affiliated with an Indian tribe qualifies for the entrepreneurs' block or as a small business. Cook Inlet has set forth several reasons why we should treat gaming revenues differently from other types of Indian tribe revenues. First, these revenues were not part of the tribal economic picture when Congress enacted the SBA tribal exception to the affiliation rule in 1970.[104] Second, the Indian Gaming Regulatory Act provides certain Indian tribes with a non-traditional source of revenue that could be very substantial.[105] Cook Inlet also asserts that gaming revenues are not subject to the same types of legal and governmental controls as other revenues received

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[98] Cook Inlet Petition for Further Clarification, filed Sept. 7, 1994, at 4.

[99] *Id.* 4-5.

[100] *Id.*

[101] *Id.*

[102] *Order on Reconsideration*, FCC 94-217 at ¶ 4.

[103] Cook Inlet *ex parte* comments, filed Oct. 31 1994, at 2.

[104] Cook Inlet *ex parte* comments, filed Oct. 31, 1994, at 2.

[105] *Id.*

by Indian tribes, and therefore are more analogous to the revenues of non-Indian entities.[106] Furthermore, Congress granted the SBA (whose rules inspired our affiliation rules) flexibility to treat tribal and other affiliations with exceptional revenues differently if such revenues would create an "unfair competitive advantage."[107] Gaming revenues generated by tribal organizations, appear to be exceptional revenues that if not included, create an unfair competitive advantage in the auctioning of broadband PCS entrepreneurs' block licenses. Thus, we will include such gaming revenues in our calculations when determining eligibility for the entrepreneurs' block and for small business status, unless the entrepreneurs' block applicant establishes that it will not receive an unfair competitive advantage, because significant legal constraints restrict its ability (or an affiliate's ability) to access and utilize revenues from gaming.

45. Finally, we decline to create an exception to our affiliation rules for rural telephone companies.[108] We are concerned that relaxing our rules would unfairly match large rural telephone companies, with greater access to capital, against entrepreneurs and designated entities (including small and medium-size rural telephone companies). We note in this regard, that rural telephone companies already enjoy substantial regulatory benefits (*e.g.*, access to Rural Electrification Administration loans, discussed *infra* at paragraph 111) affecting available capital in comparison to other designated entities.[109] Moreover, we observe that rural telephone companies will be permitted to acquire partitioned licenses at any time after the close of auctions. We believe that existing measures will thereby achieve our goal of facilitating the rapid deployment of PCS to rural areas. At MEANS/SDN's request, however, we clarify that a centralized equal access provider (*i.e.*, a group of rural telephone companies that provide centralized equal access and other sophisticated information services)[110] will not be deemed an affiliate of each of its constituent members. Based on the record, it does not appear that such entities control their constituent members or that each of the members control the centralized equal access providers. Thus, for example, if two or more of MEANS' members form a consortium of small businesses that apply for the

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[106] *Id.*

[107] As we noted in our *Order on Reconsideration*, Section 7(j)(10)(J) of the Small Business Act gives the SBA the discretion to consider tribal and other affiliations if it determines that one or more such tribally-owned businesses has obtained, or is likely to obtain, a substantial unfair competitive advantage within an industry category. *See* 15 U.S.C. § 636(j)(10)(J)(ii)(11).

[108] TEC Petition at 14-15 (requesting exemption from the affiliation rules).

[109] BET Opposition, at 16-17.

[110] *See, e.g.*, 47 C.F.R. § 69.112(i) (citing to *Transport Rate Structure and Pricing*, CC Docket No. 91-214, FCC 920442, 7 FCC Rcd 7002 (1992), *modified,* 8 FCC Rcd 5370, 5287 (1993) for description of "centralized equal access providers").

entrepreneurs' blocks, MEANS itself would not be attributed to each one of the small businesses. We agree with MEANS that this clarification will contribute to the efficient deployment of broadband PCS in rural areas.

B. Designated Entity Definitions

1. Minority and Women-Owned Businesses

46. Background. In the *Fifth Report and Order*, we adopted the definition of the term "members of minority groups" as set forth in our *Second Report and Order* in this docket.[111] Thus, we defined "members of minority groups" as ". . . individuals of African-American, Hispanic-surnamed, American Eskimo, Aleut, American Indian and Asian American extraction." [112]

47. Petition. Karl Brothers requests that the Commission amend its definition of "members of minority groups" to include businesses owned by individuals with disabilities.[113] Specifically, Karl Brothers suggest the Commission adopt the standard established in the SBA Section 8(a) program to determine who should qualify for designated entity status. According to Karl Brothers, this SBA program includes businesses owned by disabled individuals under a "means" and "socially disadvantaged" test. Karl Brothers maintains that the congressional mandate to give special preference to minority groups is not limited to just ethnic minorities, but should include other historically disadvantaged minorities. Karl Brothers maintains that Congress was merely giving examples of groups to be included in the definition of minorities, not limiting the definition to ethnic groups only. Karl Brothers contends that there is no statutory language excluding other disadvantaged groups.[114]

48. Decision. After considering Karl Brothers' request, we will not include persons with disabilities in the definition of minorities for purposes of bidding on the entrepreneurs' blocks and obtaining the special provisions available to minority applicants. The record in this proceeding does not contain any evidence that demonstrates that firms owned by persons with disabilities have more difficulty accessing capital than any other small business. In this

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[111] *See Fifth Report and Order*, FCC 94-178 at n. 157. *See also Second Report and Order*, 9 FCC Rcd 2348, 2397 n.209, *quoting Statement of Policy on Minority Ownership of Broadcasting Facilities*, 68 FCC 2d 979, 980 n.8 (1978) and *citing Commission Policy Regarding the Advancement of Minority Ownership in Broadcasting*, 92 FCC 2d 849, 849 n.1 (1982); 47 C.F.R. § 1.2110(b)(2)).

[112] *Fifth Report and Order*, FCC 94-178 at n. 157. *See* 47 C.F.R. § 24.720(i).

[113] Karl Brothers Petition for Reconsideration (Karl Brothers Petition), filed August 22, 1994, at 3.

[114] *Id.*

respect, the record of this proceeding on the difficulties that minorities, women and small businesses, in general, have experienced accessing capital strongly supports the special provisions we adopted for these groups.[115] Moreover, individuals with disabilities are not expressly named as a designated entity in Section 309(j)(4)(D) of the Communications Act, and there is no indication in the legislative record of the statute that Congress intended to expand this group of beneficiaries to include any group or individual that can demonstrate that it is "socially disadvantaged" similar to the SBA Section 8(a) approach described by the Karl Brothers.[116] Unlike the Small Business Act, Section 309(j)(4)(D) of the Communications Act does not contain the term "socially disadvantaged." *Compare* 47 U.S.C. § 309(j)(4)(D) *with* 15 U.S.C. § 637(a)(1), (4) and (5). We note that even in the SBA context, that agency presumes eligibility for Section 8(a) status for minority groups (which are defined in racial and ethnic terms), but firms owned by persons with disabilities must demonstrate that they are "socially disadvantaged" in order to gain entry into the program. Also, the SBA's denial of Section 8(a) status for firms owned by persons with disabilities where such "social disadvantage" has not been established, has been upheld in court.[117]

49. Additionally, there is no indication that in enacting Section 309(j)(4)(D) Congress intended to expand the definition of "members of minority groups" to include classes of persons other than racial or ethnic groups, such as those listed in the preceding subsection, Section 309(i).[118] We further observe that in no other Commission context, have we included disabled persons in the categories of groups that comprise our definition of minorities. Making such a change here, without clear statutory and legislative support to do so, would therefore be inconsistent with our traditional application of the definition, which we believe should be uniform in all licensing contexts.[119]

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[115] *See Fifth Report and Order*, FCC 94-178 at ¶¶ 93-112.

[116] *See* Karl Brothers Petition at 2-5.

[117] *See Doe v. Heatherly*, 671 F. Supp. 1081 (D. Md. 1978), *aff'd* 854 F.2d 1316 (4th Cir. 1988).

[118] 47 U.S.C. § 309(i)(3)(C)(ii). Below, we revise our definition of "members of minority groups" to conform to this statutory definition. In interpreting this definition in the past, we have taken a restrictive view of the categories of minorities included in this definition and limited its expansion. *See Third Report and Order,* Gen. Docket No. 81-768, 102 FCC 2d 1401 (1985).

[119] *See In re Petition of Paralyzed Veterans Of America, et. al, to Amend Regulations Facilitating Minority Ownership of Broadcast Facilities to Include the Physically Handicapped, Memorandum Opinion and Order,* FCC 85-651, 59 Rad. Reg. 2d (P&F) 1353 (released Dec. 16, 1985), *petition for review dismissed as untimely, California Assoc. of the Physically Handicapped, Inc. v. FCC*, 833 F.2d 1333 (9th Cir. 1987).

50. We wish to emphasize also, that it is highly likely that most firms owned by individuals with disabilities will be eligible to bid in the entrepreneurs' block and for an installment payment option if they meet the required gross revenues and total assets test. Such firms may also be eligible for "enhanced" installment payments and bidding credits if they qualify as small businesses under our rules. Indeed, absent a substantial record that demonstrates firms owned by persons with disabilities have any more difficulty accessing capital than any other small business, we find that we cannot accommodate the Karl Brothers request.

51. We also note that we have before us a Petition for Rulemaking filed by David J. Lieto (Lieto Petition), which requests that the Commission amend Section 1.2110 of the Commission's rules to provide that disabled individuals are within the minority group categories and are thus entitled to the benefits associated with being a designated entity under the Commission's auction rules.[120] As stated above, we believe that our existing rules provide opportunities for individuals with disabilities to participate in the entrepreneurs' block, and that there is no direct statutory or record support for Lieto's request. Furthermore, Lieto has failed to provide a record comparable to that for women and minorities demonstrating that disabled individuals experience difficulties accessing capital that are unique to their status. Accordingly, we decline to initiate a rulemaking at this time, and hereby dismiss the Lieto Petition.

52. In response to numerous inquiries,[121] however, we revise the definition of "members of minority groups" slightly to conform with the definition of minority used in other contexts. [122] Thus, Section 24.720(i) of the Commission's rules shall read as follows: "Members of minority groups include Blacks, Hispanics, American Indians, Alaskan Natives, Asians, and Pacific Islanders."[123] We have also been asked to clarify the meaning of

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[120] *See* David J. Lieto Petition for Rulemaking, filed September 21, 1994, at 2-3.

[121] We received several inquiries about the definition of "members of minority groups" from participants in the FCC PCS seminars, which provided an overview of the PCS rules and procedures. The seminar series included sessions held in the following locations: Washington, D.C. (Aug. 29, 1994); Chicago (Aug. 22, 1994); Denver (Aug. 24, 1994); San Francisco (Aug. 26, 1994).

[122] *See, e.g., Broadcast Equal Employment Opportunity Rules and FCC Form 395*, 70 FCC 2d 1466, 1473 (1979); 47 C.F.R. §§ 73.3555(d)(3)(iv), 1.1621(b); *see also* 47 U.S.C. § 309(i)(3)(c)(ii); Race and Ethnic Standards for Federal Statistics and Administration Reporting, OMB Statistical Policy Directive No. 15 (1977).

[123] In a separate *Order*, we shall be making the same correction to the definition of minority groups used in the generic auction rules (*see* 47 C.F.R. § 1.2110(b)(2)) and the narrowband auction rules (*see* 47 C.F. R. § 24.320(f)).

particular categories in the definition of minority. Again, for consistency, we shall use the same category descriptions the Commission has relied on in other contexts.[124] These categories are as follows :

a. Black. A person having origins in any of the black racial groups of Africa.

b. Hispanic. A person of Mexican, Puerto Rican, Cuban, Central or South American or other Spanish Culture or origin, regardless of race.

c. American Indian or Alaskan Native. A person having origins in any of the original peoples of North America, and who maintains cultural identification through tribal affiliations or community recognition.

d. Asian or Pacific Islander. A person having origins in any of the original peoples of the Far East, Southeast Asia, the Indian subcontinent, or the Pacific Islands. This area includes, for example, China, India, Japan, Korea, the Philippine Islands, and Samoa.

To address any specific claims or allegations regarding an individual race or origin, we will follow existing Commission precedent.[125] To the extent that prior Commission cases do not provide adequate guidance in specific cases, we may look to cases developed under minority programs in other federal agencies, such as the Office of Management and Budget (OMB) and the SBA.

2. Small Business Consortia

53. Background. In the *Fifth Report and Order* the Commission allowed a consortium of small businesses to qualify collectively for the preferences available to a small business if each business within the consortium individually satisfies the definition of a small business designated entity.[126] The Commission defined a small business designated entity as any company that, together with attributable investors and affiliates, has average gross revenues for the three preceding years of not in excess of $40 million.[127] We defined "consortium of small businesses" as a conglomerate organization formed as a joint venture

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[124] *See Broadcast Equal Employment Opportunity Rules and FCC Form 395*; *see also* "Instructions for Completing FCC Forms 395-A & 395-M," Section V (Race/Ethnic Categories).

[125] *See, e.g., Lone Cypress Radio Assoc. Inc.,* 7 FCC Rcd 4403 (Rev. Bd. 1992), and cases cited therein; *See also Storer Broadcasting Co.,* 87 FCC 2d 190, 191-93 (1981).

[126] *Fifth Report and Order*, FCC 94-178 at ¶ 180. *See also* 47 C.F.R. § 24.720(b)(3)).

[127] *Fifth Report and Order*, FCC 94-178 at ¶ 175. *See also* 47 C.F.R. § 24.720(b)(1).

among mutually-independent business firms, each of which individually satisfies the definition of a small business.[128] In the *Second Report and Order,* we concluded that consortia should not always be entitled to qualify for measures designed specifically for designated entities.[129] In the *Fifth Report and Order*, however, we stated that for the auctioning of broadband PCS, it is especially necessary to allow small businesses to pool their resources in this manner to help them overcome capital formation problems.[130] Thus, our rules provide that if a consortium's members are all small businesses (*i.e.*, defined as companies that do not have average yearly gross revenues for the preceding three years in excess of $40 million), the consortium as a whole will qualify for designated entity provisions for small businesses.

54. Petitions. Omnipoint requests that the Commission allow small businesses to form a single corporate applicant (rather than a joint venture) and get the same treatment as consortia.[131] BET requests that the Commission eliminate the preferences available to small business consortia.[132]

55. Decision. We believe the current preferences for small business consortia are adequate and necessary to ensure that small businesses have sufficient opportunities to participate in the broadband PCS auctions. Accordingly, we deny BET's request to eliminate the small business consortia preferences. As we observed in the *Fifth Report and Order*, allowing small businesses to pool their resources in this manner is necessary to help them overcome capital formation problems and ensure their participation in the provision of broadband PCS. We believe that small, rural telephone companies, in particular, are expected to use this mechanism to compete in some of the smaller markets.

56. We also deny Omnipoint's request that small businesses be allowed to form a single corporate applicant that would be afforded the same treatment as consortia. The concept of a consortium is that each small business participant remains a distinct corporate entity independent of other consortium members and that each member has rights and obligations similar, or equal to, those held by participants in other types of joint ventures. Allowing a group of small businesses to apply as one corporate applicant and receive the benefits of our consortia rule would disadvantage small, independent businesses wishing to bid as a group under our rule, but who cannot restructure as a corporate applicant and could tend to dilute each member's influence and insulate their responsibilities in the venture. We

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[128] *Fifth Report and Order*, FCC 94-178 at ¶ 179. *See also* 47 C.F.R. § 24.720(b)(3).

[129] *Second Report and Order*, FCC 94-61 at ¶ 286.

[130] *Fifth Report and Order*, FCC 94-178 at ¶ 180.

[131] Omnipoint Petition at 9.

[132] BET Petition at 7.

believe that such a change would also eviscerate our small business eligibility size requirement. We wish to clarify, however, that we intend to examine the qualifications of each consortium member to ensure that each is a *bona fide* small business. In this regard, it is assumed that each concern should be an entity "organized for profit" and not for the sole purpose of qualifying as part of a small business consortia. This is consistent with SBA's long-standing definition of "business concern." *See* 43 C.F.R. § 121.403(a), *Small Business Size Standards*, 54 Fed. Reg. 52634 (Dec. 21, 1989).

57. On another issue, BET contends that the $40 million gross revenues standard fails to comply with an SBA requirement that any size standard proposed by a federal agency that varies from SBA's standard be "proposed after an opportunity for public notice and comment" and be "approved by the Administrator [of the SBA]."[133] We believe we have fully met our notice and comment obligations, both under the Administrative Procedures Act and the Small Business Act, in this proceeding. We solicited comment on a range of size options, and received comment that included SBA's recommendation for a $40 million gross revenues cap (which we ultimately adopted). Indeed, we recently obtained SBA's approval of the $40 million size standard.[134]

C. Eligibility Requirements

1. Minimum Equity Limit for the Control Group

58. Background. In the *Fifth Report and Order*, the Commission adopted a methodology for assessing an applicant's compliance with the financial caps for the entrepreneurs' blocks and for small business size status based on the distinction between: (a) noncontrolling investors (whose financial status would not be attributed to the applicant); and (b) investors holding interests in the control group of the applicant.[135] The gross revenues, assets and personal net worth limits of attributable investors (*i.e.*, those with more than 25 percent equity) and *all* control group members, regardless of the size of their individual interests, are included in assessing an applicant's compliance with the financial caps.[136] To qualify as a women or minority-owned business, the Commission further required that the control group be composed entirely of women and minorities.[137] The control group

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[133] *See* 15 U.S.C. § 632(a)(2)(A) and (C). BET Reply to Oppositions to Petitions for Reconsideration, filed Sept. 22, 1994, at 7-8.

[134] *See* Letter to William Kennard, FCC General Counsel, from Philip Lader, SBA Administrator, Nov. 9, 1994 (responding to Aug. 19, 1994 request for size approval).

[135] *Fifth Report and Order*, FCC 94-178 at ¶¶ 158-59.

[136] *Id. See also Order on Reconsideration*, FCC 94-217 at 5-6.

[137] *Fifth Report and Order,* FCC 94-178 at ¶¶ 160-62, 181-92.

requirement ensures that designated entity and entrepreneur principals retain control of the applicant and own a substantial financial interest in the venture. At the same time, it enables noncontrolling investors outside the control group to provide essential capital to an applicant without their revenues, assets or net worth being attributed to the applicant or their non-minority or male status disqualifying the applicant.

59. The Commission adopted two control group options in the *Fifth Report and Order*.[138] Under the first option, passive investors are permitted to own up to 75 percent of the applicant's total equity, so long as: (1) no investor holds more than 25 percent of the applicant's passive equity (which was subsequently defined to include up to 15 percent of a corporation's voting stock); and (2) in the case of a corporate applicant, at least 50.1 percent of the voting stock is held by the control group.[139] In the case of partnership applicants, the control group must own all the general partnership interests.[140] The Commission determined that this minimum equity level strikes an appropriate balance between the competing considerations of permitting qualified bidders to raise capital and ensuring that designated entities receive a significant economic benefit from the venture.[141] The Commission extended an alternate option to qualified women or minority-owned businesses. Under this option, the Commission would permit a single investor in a women or minority-owned applicant to own up to 49.9 percent of the passive equity (which we subsequently defined to include up to 15 percent of a corporation's voting stock), so long as the control group holds the remaining 50.1 percent of the equity. As with the first option, the control group is required to retain control and, in the case of a corporate applicant, hold at least 50.1 percent of the voting stock.[142] Also, ownership interests are to be calculated on a fully diluted basis .

60. Petitions. Petitions filed by BET, Columbia PCS, CTIA, EATEL, Lehman Brothers and Omnipoint variously address the Commission's restrictions on the composition of an applicant's control group.[143] Specifically, petitioners request clarification that our attribution rules and definitions of minority and women-owned business be interpreted to

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[138] *Id.* at ¶¶ 158-163. As discussed *infra* at ¶ 65, one of the options is available only to women and minority-owned businesses.

[139] *Id.* at ¶ 158.

[140] *Id.*

[141] *Id.* at ¶ 159.

[142] *Id.* at ¶ 160. *See Order on Reconsideration*, FCC 94-217 at ¶ 10.

[143] BET Petition at 15-16; Columbia PCS Petition at 2-5; CTIA Petition at 4-10; EATELCORP, Inc. Petition for Reconsideration, (EATEL Petition), filed Aug. 22, 1994, at 3-7; Lehman Brothers Petition for Reconsideration (Lehman Bros. Petition), filed Aug. 22, 1994, at 4-5; Omnipoint Petition at 15-16.

permit "nonqualifying" noncontrolling investors *within* the control group.[144] "Nonqualifying" investors, as petitioners describe, are investors that are neither women nor minorities, or investors that if attributed would cause the applicant to exceed the financial caps. EATEL argues that to do otherwise may preclude participation by existing companies whose existing corporate structures would disqualify an applicant absent significant expenditures for corporate restructuring. EATEL maintains that existing entities have the greatest amount to offer applicants in terms of financial and technical resources.[145] Petitioners also request that the Commission allow a limited amount of equity investment in the control group to help the applicant comply with the 25 percent minimum equity requirement. Columbia PCS, for example, advocates adoption of a bright-line test that would require at least a 75 percent equity and a 100 percent voting interest in the control group to be held by "qualifying" entities.[146] Columbia PCS maintains that designated entities will be unable to raise sufficient capital unless this clarification is made.[147] EATEL and CTIA maintain that the 100 percent equity requirement for minority and women-owned control groups is too restrictive for entities already in existence. Instead, they argue that businesses which are in fact *controlled* by women and/or minorities, but which have numerous non-controlling shareholders (including some that are neither women nor minorities), should be eligible for the preferences we adopted for minority and women-owned businesses.[148] BET also requests clarification that a control group may be comprised of a single individual.[149]

61. Omnipoint, Columbia PCS, CTIA and Lehman Brothers contend that the 25 percent minimum equity ownership restriction is too high and that designated entities will face insurmountable difficulties arranging financing if it is not reduced.[150] To remedy this problem, Lehman Brothers proposes two alternative solutions. First, for publicly-traded companies, Lehman proposes that public shareholders with less than 5 percent equity should be counted towards the control group's 25 percent equity threshold. Lehman maintains that this proposal would permit control group equity to be diluted by new shareholders, but not

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[144] BET Petition at 16; Columbia PCS Petition at 2-4; EATEL Petition at 2-4; Lehman Bros. Petition at 4-5; Omnipoint Petition at 16.

[145] EATEL Petition at 5-6.

[146] Columbia PCS Petition at 2-4.

[147] *Id.* at 2.

[148] EATEL Petition at 6-7; CTIA Petition at 9-10.

[149] BET Petition at 16.

[150] Omnipoint Petition at 9-10; Lehman Bros. Petition at 3; Columbia PCS Petition at 2.

below a minimum equity level (Lehman recommends 10 percent).[151] Second, Lehman suggests that all designated entities should be permitted to dilute their 25 percent equity interests in the following circumstances: (a) not earlier than one year after license grant, to dilute control group equity to a total of not less than 20 percent; (b) not earlier than two years, to dilute control group equity to a total of not less than 15 percent; and (c) not earlier than three years to dilute control group equity to a total of not less than 10 percent. Lehman argues that this proposal would provide designated entities efficient access to capital, thereby improving their competitive position.[152] CTIA recommends that an applicant should be eligible to bid on the C and F blocks with at least 10 percent equity.[153] Lehman Brothers also requests that the Commission modify its control group definition to provide that members of the control group receive dividends, profits and regular and liquidating distributions in proportion to the actual possession of equity held, rather than in proportion to their interest in the total equity of the applicant. Lehman Brothers contends that our rules could be interpreted to mean that such distributions must be paid on options held but not exercised by control group members, rather than on the basis of actual shares held.[154]

62. Decision. After considering the record, and as described below, we modify our rules to allow certain noncontrolling investors who do not qualify for the entrepreneurs' block or as a small business to be investors in an applicant's control group. We also allow entities that are controlled by minorities and/or women, but that have investors that are neither minorities nor women, to be part of the control group. We agree with petitioners that some accommodation should be made in our regulations to allow participation in an applicant's control group by existing firms controlled by designated entities or entrepreneurs that have investors that, if attributed, would cause the applicant to exceed the small business or entrepreneurs' blocks financial caps or, for minority or women-owned applicants, investors that are not minorities or women.[155] We will therefore modify our definition of a minority and women-owned business to include preexisting companies that are controlled by women or minorities but have noncontrolling investors in the control group who are not minorities or women. Similarly, we will allow preexisting companies that, in aggregate, meet our entrepreneurs' block and small business size standards to be members of the control group even if one or more of the noncontrolling investors in those companies would disqualify the company based on its gross revenues or total assets. We believe that these rule

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[151] Lehman Bros. Petition at 4. *See also* Impulse *ex parte* comments, filed Oct. 12, 1994, at 1-4 (arguing that a 25% minimum equity requirement, if maintained throughout the life of the venture, would severely limit normal capital formation by designated entities).

[152] *Id.* at 5.

[153] CTIA Petition at 9.

[154] *See* Lehman Bros. Petition at 6-8. *See also* 47 C.F.R. § 24.720(k)(iv).

[155] EATEL Petition at 5-7; Columbia PCS Petition at 2-4.

changes will provide a reasonable balance between the need to ensure that designated entities have a significant economic investment in the applicant and the financing realities of a PCS venture.

63. We also agree with petitioners that it is not optimal to require the qualifying control group members to hold at least 25 percent of the applicant's equity. The record indicates that in many cases, designated entities and entrepreneurial principals will have limited capital to contribute to the applicant's equity and that noncontrolling investors will be unwilling to advance funds to enable the designated entity (even one with management expertise) to reach the 25 percent threshold.[156] Thus, without some modifications to our rules, designated entities could face insurmountable difficulties in arranging financing. We therefore conclude that we should modify our rules to address petitioners' concerns, while balancing the need to ensure meaningful equity participation by "qualifying" control group members.[157]

64. Specifically, we will retain the 25 percent minimum equity requirement for the control group, but we will require only 15 percent (*i.e.*, 60 percent of the control group's 25 percent equity contribution) to be held by qualifying, controlling principals in the control group (*i.e.*, minorities, women or small/entrepreneurial business principals).[158] For example, if the applicant seeks minority or women-owned status, the 15 percent equity (as well as 50.1 percent of the voting stock of the applicant) must be owned by control group members who are minorities and/or women. If the applicant seeks small business status, 15 percent of the equity must be held by control group members who, in the aggregate, qualify as a small business.[159] The composition of the principals of the control group determines whether the applicant qualifies for bidding credits, installment payments and reduced upfront payments. The 15 percent may be held in the form of options, provided these options are exercisable at any time, solely at the holder's discretion, and at an exercise price equal to or less than the current market valuation of the underlying shares at the time of short-form filing. The

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[156] AirTouch *ex parte* comments, filed Oct. 12, 1994, at 2; Columbus Grove Telephone Co., *ex parte* comments, filed Oct. 5, 1994, at 2.

[157] *See* Appendix C (chart illustrating changes to the control group's voting and ownership thresholds).

[158] *See* Media Communications Partners *ex parte* comments, filed Oct. 11, 1994, at 7-8.

[159] For instance, if a preexisting company wants to qualify as a small business control group, its gross revenues and total assets will be added to the gross revenues and assets of each of its controlling shareholders and to those of all affiliates. The resulting sum must be under $40 million in gross revenues and $500 million in total assets. The gross revenues and total assets of the company's preexisting, noncontrolling shareholders will be ignored, however.

remaining 10 percent (*i.e.*, 40 percent of the control group's minimum equity contribution) may be held in the form of either stock options or shares, and we will allow certain investors that are not minorities, women, small businesses or entrepreneurs to hold interests in such shares or options. Specifically, we will allow the 10 percent portion to be held in the form of shares or stock options by: (1) investors in the control group that are women, minorities, small businesses or entrepreneurs; (2) individuals who are members of an applicant's management team (which could include individuals who are not minorities or women or individuals who have affiliates that exceed the entrepreneurs' block or small business size thresholds); (3) existing investors of businesses in the control group that were operating and earning revenues for two years prior to December 31, 1994; or (4) noncontrolling institutional investors.[160]

65. As discussed *supra* at paragraph 59, the Commission also adopted an alternative to the 25 percent minimum equity requirement for minority and women-owned businesses, which permits a single investor to hold as much as 49.9 percent of its equity, provided the control group holds at least 50.1 percent. Several petitioners have expressed similar concerns with respect to the need to revise the 50.1 percent requirement.[161] Therefore, in tandem with, and for the same reasons as, the modifications to the 25 percent equity requirement, we make similar modifications to the rules governing the 50.1 percent minimum equity requirement. Accordingly, where a minority or women-owned business uses the 50.1 percent minimum equity option, we will require only 30 percent of the total equity to be held by the principals of the control group that are minorities or women. The 30 percent may be held in the form of options, provided these options are exercisable at any time, solely at the holder's discretion, and at an exercise price equal to or less than the current market valuation of the underlying shares at the time of short-form filing. The remaining 20.1 percent may be made up of shares and/or options held by investors that are not women or minorities under the same criteria described in paragraph 64 above. That is, the 20.1 percent portion of the control group's equity may be held in the form of shares or stock options by any of the following: (1) investors in the control group that are minorities, women, small businesses or entrepreneurs; (2) individuals who are members of an applicant's management team (which could include individuals who are not minorities or women, or individuals who have affiliates that exceed the entrepreneurs' block and small business size standards); (3) existing investors of businesses in the control group that were operating and earning revenues for two years prior to December 31, 1994; or (4) noncontrolling institutional investors.[162]

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[160] *See* note 162 *infra* (explaining definition of institutional investors).

[161] *See, e.g.*, BET Petition at 16; Columbia PCS Petition at 2-3; Omnipoint Petition at 9.

[162] For our purposes, we define institutional investors in a manner that is similar to the definition that is used by the Commission in the attribution rules applied to assess compliance with the broadcast multiple ownership rules. We modify that definition slightly, however, to fit this service. Specifically, we expect that investment companies will be important sources

66. In addition, the control group minimum equity requirement will be reduced three years from the date of license grant as suggested by Lehman Brothers, but the control group must still retain voting control (*i.e.*, 50.1 percent of the vote).[163] According the control group the option to reduce the equity requirement accommodates the needs of designated entity licensees to raise capital as they build out their systems.[164] Significantly, the three-year mark corresponds with the end of the no transfer period under our license holding rule. In the case of a licensee that has chosen the 25 percent minimum equity option, the principals in the control group will only be required to hold 10 percent of the licensee's equity after three years, with no further equity requirements imposed on the control group. Similarly, in the case of a licensee that has used the 50.1 percent minimum equity option, the principals in the control group will be required to hold 20 percent of the licensee's equity, and no further equity requirements will be imposed on the control group.

67. After reviewing the record, we are persuaded that these changes will afford the control group greater flexibility in raising the necessary equity for participation in the entrepreneurs' blocks. In particular, we are allowing that 10 (or 20.1) percent of the equity can come from sources that otherwise would not qualify for the control group. In making these limited changes to the control group equity requirements, we believe the amended rules will: (1) promote investment in designated entities generally; (2) attract and promote skilled management for applicants; and (3) encourage involvement by existing firms that have valuable management skills and resources to contribute to the success of applicants.

68. With respect to our decision to allow investment in the control group by investors of preexisting firms, the business involved must be a going concern that has been in existence for a reasonable period of time prior to adoption of our rules in order to avoid any sham arrangements. Specifically, the business involved must have been operating and

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of capital formation for designated entities. Accordingly, we adopt a definition that specifically includes venture capital firms and other smaller investment companies that may not be included in the definition of investment companies found in 15 U.S.C. § 80a-3 (which is cited in our broadcast rules at 47 C.F.R. § 73.3555 Note 2(c). Specifically, we define an *institutional investor* as an insurance company, a bank holding stock in trust accounts through its trust department, or an investment company as defined in 15 U.S.C. § 80a-3(a), without reference to, or incorporation of, the exemptions set forth in 15 U.S.C. §§ 80a-3(b) and (c); provided that, if such investment company is owned, in whole or in part, by other entities, then such investment company, such other entities and the affiliates of such other entities, taken as a whole, must be primarily engaged in the business of investing, reinvesting or trading in securities or in distributing or providing investment management services for securities. *See* Section 24.720(h).

[163] *See* Lehman Bros. Petition at 4-5.

[164] *See id.* at 2-4.

earning revenues for at least two years prior to December 31, 1994 to qualify for this provision. While we want to relax the control group equity requirements slightly, we also recognize there may be an incentive for nonqualifiying investors to purchase substantial interests in "preexisting" businesses unless we place some restrictions on those investors. As a practical matter, however, we realize that the identity of noncontrolling investors in such businesses, particularly if they are publicly-traded companies, will change regularly. As we state *infra* in our discussion on the treatment of preexisting businesses that are the sole control group member, we intend that the allowed equity (10 or 20.1 percent) portion should be held by existing investors in such a company although we will not place limits on who qualifies as such an investor. We emphasize, however, that we will scrutinize any significant equity restructuring of preexisting companies that occurs after adoption of our rules. We would presume that any change of equity by an investor in a preexisting company (that is in an applicant's control group) that is five percent or less would not be significant, and the burden is on the applicant to demonstrate whether changes in equity that exceed five percent are *not* significant.

69. We also agree with petitioners and commenters that greater flexibility should be afforded to any applicant whose ownership structures were established before our designated entity requirements were formulated.[165] Therefore, as a further modification, if the sole control group member of an applicant is a business that was in existence and had earnings from operations for at least two years prior to December 31, 1994, we offer the option that control group principals establishing the applicant's status as a minority and/or women-owned business, small or entrepreneurial business may hold 10 percent of the applicant's equity if the 25 percent equity option is used, or a 20 percent equity interest if the 50.1 percent equity option is used.[166] The balance of the control group's equity contribution (*i.e.*, 15 or 30.1 percent) must be held in the form of shares or stock options by any of the following: (1) qualifying principals in the control group; (2) individuals who are members of the applicant's management team (which could include "nonqualifying" individuals); or (3) existing investors of businesses in the control group that were operating and earning revenues for two years prior to December 31, 1994.

70. The lower equity requirement of 10 percent for preexisting companies that are sole control group members addresses the concerns of these firms, many of which have already undergone successive rounds of financing that may have diluted the qualifying investors' original equity interest in the business. Existing firms that were structured prior to

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[165] *See, e.g.*, BET Petition at 12-15; CTIA Petition at 8-9; EATEL Petition at 2-3; MEANS/SDN Opposition at 10.

[166] As described *supra* at ¶ 65, this equity may be held outright or in the form of options provided these options are exercisable at any time, solely at the holder's discretion, and at an exercise price equal to or less than the current market valuation of the underlying shares at the time of the filing of the short-form application.

the adoption of the entrepreneurs' block regulatory scheme are less likely to become "fronts" for businesses that would not qualify for the entrepreneurs' blocks or the special provisions accorded designated entities. This option is solely intended to accommodate long-standing capital structures of applicants that have already been required to dilute equity ownership to raise capital. Thus, we will require that the portion of equity not held by qualifying principals (15 or 30.1 percent, as the case may be) to be comprised entirely of existing investors of the company (unless the equity is held by management or qualified principals of the control group). As we stated above, we recognize that for many companies, especially those that are publicly-traded, the identities of noncontrolling investors change regularly. Thus, as stated *supra,* we will not place limits on the amount of time a particular individual or entity must have been an investor in the company. We emphasize, however, that we will scrutinize carefully applicants that engage in significant equity reshuffling after adoption of our rules.[167] By giving preexisting applicants additional flexibility, we do not intend to place other applicants at a competitive disadvantage by permitting greater capital infusion from institutional investors.[168]

71. In implementing our requirements, we will provide that where the interests in question are not held directly in the applicant, a multiplier will be used to calculate the effective interests held by the control group principals toward fulfillment of the minimum equity requirement. In addition, we will use a multiplier to calculate the interests of noncontrolling investors in the control group so as to assess compliance with the 25 percent nonattributable equity limit.[169] A multiplier is a traditional tool used by the Commission to calculate the effective ownership levels of investors that, through one or more intervening

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[167] As stated *supra* at ¶ 68, we will presume that a change in equity by an investor (in a preexisting business) of five percent or less is not significant, and the burden is on the applicant to demonstrate whether equity changes above five percent are *not* significant.

[168] *See* BET *ex parte* comments, filed Nov. 3, 1994, at 2-4.

[169] We illustrate the application of a multiplier as follows: If a member of a minority group or a woman holds a 25 percent equity interest in a corporate member of the control group and that corporation holds a 25 percent equity interest in the applicant, the effective interest for purposes of assessing compliance with the minimum equity requirement would be 6.25 percent (*i.e.*, 0.25 x 0.25 = 6.25). This falls well below the 25 percent requirement of our original rule. Correspondingly, if a noncontrolling (and nonqualifying) investor holds a 40 percent interest in a corporate member of a control group and that corporation holds 25 percent of the applicant's total equity, the effective interest held in the applicant by the investor would be 10 percent (*i.e.*, 0.25 x .40 = 10.00). If that same investor also owns more than 15 percent of the applicant's equity outside of the control group, it would exceed the 25 percent nonattributable equity limit.

corporations, hold indirect interests in a licensee.[170]

72. Additionally, in a written *ex parte* presentation, Metricom requests that we exempt small, publicly-traded corporations with widely dispersed voting stock ownership from our control group requirement.[171] Metricom contends that the control group concept is unworkable for small, publicly-traded companies, because it would not be possible to identify a group of shareholders that own 50.1 percent of the corporation's voting stock.[172] As a result, such corporations could be unable to establish eligibility for the entrepreneurs' blocks, or status as a small business. Metricom proposes a test for identifying small, publicly-traded corporations with widely dispersed voting stock ownership that closely follows guidelines used by the Securities and Exchange Commission.[173]

73. We will adopt Metricom's proposal, and create a limited exemption from the control group requirement for small, publicly-traded corporations with widely dispersed voting stock ownership. As Metricom points out, a significant number of small, publicly-traded companies have such widely dispersed voting stock ownership that no identifiable control group exists or can be created.[174] Without a control group, such companies may not be able bid for entrepreneurs' block licenses or qualify for small business status even though their gross revenues and assets meet our financial caps. It was not the Commission's intent that these companies be denied the opportunity to bid on the entrepreneurs' block, or to qualify for treatment as a small business.

74. Consistent with Metricom's proposal, a small, publicly-traded corporation will be found to have dispersed ownership of voting stock if no person (including any "group" as

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[170] *See, e.g.*, 47 C.F.R. § 73.3555 Note 2(d) (indicating that attribution ownership interests in a broadcast licensee, cable television system or daily newspaper that are held indirectly by a party through one or more intervening corporations will be determined by successive multiplication of the ownership percentages for each link in the vertical ownership chain). We note that the multiplier used here does not employ the 51 percent control exception used in the broadcast context since we are using a multiplier only to determine a control group member's equity investment, not whether such member has control or substantial influence over the applicant.

[171] Metricom, Inc. *ex parte* comments, filed Oct. 20, 1994.

[172] *Id.* at 6-7.

[173] *Id.* at 10-11.

[174] *See id.* at 6-7.

that term is used in the Securities Exchange Act of 1934)[175] has the power to control the election of more than 15 percent of the corporation's directors. In addition, we will require that no person shall have an equity interest in the applicant of more than 15 percent, which is consistent with our revised equity requirements for small business applicants utilizing a control group. Under those requirements, discussed *supra* at paragraph 64, small business principals in an applicant's control group must hold at least a 15 percent interest in the applicant (in combination with an additional, 10 percent equity interest that may come from "nonqualifying" sources). A 15 percent equity requirement is appropriate here because the same percentage of equity is needed for a small business applicant's control group to satisfy its equity obligations (unless it is a preexisting company), and because a 15 percent equity cap is likely to ensure that no control questions arise. We emphasize that this control group exemption will only apply to an applicant or licensee that is not controlled by any entity or group other than corporate management, as should be the case where there is no identifiable group of shareholders holding a controlling interest in the company's voting stock. A small corporation that has dispersed voting stock ownership and no controlling affiliates will therefore not be required to aggregate with its own revenues and assets the revenues and assets of management and shareholders for purposes of entrepreneurs' block eligibility or small business status.

75. Small, publicly-traded corporations that choose to exempt themselves from the control group requirement must own all the equity and voting stock of the applicant or licensee. We find their ability to rely on the corporation's existing capital structure to introduce new passive investment on an ongoing basis provides a level of flexibility that is comparable to applicants/licensees with an identifiable control group. We note that minority and/or women-owned businesses would not qualify for this exemption since a control group is necessary to determine whether the applicant is controlled by minorities or women.

76. Finally, we consider a few other points. First, as BET requests, we clarify that an individual can be the control group of an applicant, so long as our equity requirements and other provisions are satisfied. In response to Lehman Brothers' concerns, we clarify the control group requirements to provide that control group investors must receive dividends, profits, and regular and liquidating distributions in proportion to their actual possession of equity holdings, rather than in proportion to their interest in the total equity (which may include options not yet exercised). Finally, we see no conflict in our rules with a Pacific Telesis' proposal to allow designated entities and their partners to allocate amongst

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[175] *See id.* at 10-11; *see also* 15 U.S.C. § 78(a) *et seq.* (Section 13(d) and Section 13(g) state that "when two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities in an issuer, such syndicate or group shall be deemed a 'person' and therefore required to make the disclosures indicated in those subsections").

themselves tax benefits on a non-pro rata basis.[176]

2. *De Facto* Control Issues and Management Contracts

77. In the *Fifth Report and Order*, we provided that the designated entity control group must have *de facto* as well as *de jure* control of the applicant and must be prepared to demonstrate that it controls the enterprise.[177] The requirement of *de facto* control arises from Section 310(d) of the Communications Act, which prohibits any transfer or assignment of license or transfer of control of a corporation holding a license without the Commission's authorization.[178] To help in determining what constitutes a transfer of control under this statutory provision, we follow precedent defining *de facto* control.[179] We also apply this standard in the case of designated entities to determine whether the applicant is in fact controlled by qualifying individuals or entities. Several petitioners seek reconsideration or clarification of our *de facto* control standard, particularly as it applies to questions of *de facto* control by the designated entity control group and use of management contracts by licensees.[180]

a. Definition of *De Facto* Control

78. Background. The *Fifth Report and Order* does not set forth specific guidelines defining *de facto* control in the entrepreneurs' block context. Because issues of *de facto* control are necessarily fact-specific, we have treated the issue as one to be handled on a case-by-case basis.[181] Consequently, a wide variety of factors may be relevant to determining whether a control group has *de facto* control of a particular applicant, applying in the entrepreneurs' blocks.

79. Petitions. Some petitioners ask us to provide more specific guidelines with respect to what does and does not constitute *de facto* control. Omnipoint states that such

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[176] *See* Pacific Telesis *ex parte* comments, dated Oct. 19, 1994, at 4.

[177] *Fifth Report and Order*, FCC 94-178 at ¶¶ 115, 164; 47 C.F.R. § 24.720(k).

[178] 47 U.S.C. § 310(d).

[179] *See Rochester Telephone v. United States*, 23 F. Supp. 634, 636 (S.D.N.Y. 1938), *aff'd*, 307 U.S. 125 (1939); *Lorain Journal Co. v. FCC*, 351 F.2d 824, 827-828 (D.C. Cir. 1965), *cert. denied*, 383 U.S. 967 (1966).

[180] *See* discussion *infra* at ¶¶ 79, 84.

[181] *Stereo Broadcasters, Inc.*, 55 FCC 2d 819, 821 (1975), *modified*, 59 FCC 2d 1002 (1976).

guidelines would help designated entity applicants in setting up their management structure.[182] Others seek assurance that designated entity control groups can meet the *de facto* control test even if they enter into agreements containing "standard" covenants for the protection of non-majority or non-voting shareholders, *e.g.*, supermajority voting requirements for major corporate changes, liquidation preferences (commonly in the form of preferred stock), rights of first refusal, veto rights concerning particular corporate transactions, or the preemptive right to purchase stock to prevent dilution.[183]

80. Decision. We continue to believe that determinations of *de facto* control for purposes of determining designated entity eligibility for entrepreneurs' blocks are inherently factual and therefore will require case-by-case determination. Nevertheless, to provide a level of certainty for designated entities and to ensure that designated entities maintain *de facto* control, we believe it is appropriate to articulate some guidelines for defining *de facto* control in this context. We therefore clarify that a designated entity or entrepreneurs' control group must demonstrate at least the following indicia of control to establish that it retains *de facto* control of the applicant: (1) the control group must constitute or appoint more than 50 percent of the board of directors or partnership management committee; (2) the control group must have authority to appoint, promote, demote and fire senior executives that control the day-to-day activities of the licensee; (3) the control group must play an integral role in all major management decisions; and (4) in the case of applicants controlled by minorities and women, at least one minority or female control group member must have senior managerial responsibility over day-to-day operations, *e.g.*, as President or CEO of the licensee.[184] We emphasize, however, that these criteria are guidelines only and are not necessarily dispositive of the issue of *de facto* control in all situations. Even where these criteria are met, therefore, the determination of whether *de facto* control exists will depend on the totality of circumstances in the particular case.

81. With respect to provisions benefitting non-majority or non-voting shareholders, we recognize that inclusion of such provisions is a common practice to induce investment and

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[182] Omnipoint Petition at 11-12.

[183] *See* Media Communications Partners *ex parte* comments, filed October 11, 1994; Pacific Telesis *ex parte* comments, filed October 19, 1994.

[184] These same four indicia will be used to determine whether the "qualified" members of the control group (*i.e.*, women, minorities, and small business or entrepreneurial principals) have *de facto* control over the control group. For example, in a women-owned limited partnership applicant with one corporate general partner, the women shareholders of that corporation must constitute, or be able to appoint more than 50 percent of the board, appoint, promote, demote and fire senior executives, play an integral role in all major management decisions, and at least one of the women must have senior managerial responsibility over day-to-day operations.

ensure that the basic interests of such shareholders are protected. For example, many corporations require a supermajority of shareholders to approve major corporate decisions such as taking on additional debt, significant corporate acquisitions, or issuance of new stock. Similarly, strategic investors making large passive equity contributions to a company frequently insist on a right of first refusal exercisable in the event that a third party seeks to purchase the company. We agree with petitioners that allowing such provisions enhances the ability of designated entities to raise needed capital from strategic investors, thereby bolstering their financial stability and competitive viability.[185] We believe, however, that precedent provides guidance in determining the appropriate extent to which these safeguards may protect investment.[186] We therefore clarify that under our case law non-majority or non-voting shareholders may be given a decision-making role (through supermajority provisions or similar mechanisms) in major corporate decisions that fundamentally affect their interests as shareholders without being deemed to be in *de facto* control.[187] Such decisions generally include: (1) issuance or reclassification of stock; (2) setting compensation for senior management; (3) expenditures that significantly affect market capitalization; (4) incurring significant corporate debt or otherwise encumbering corporate assets; (5) sale of major corporate assets; and (6) fundamental changes in corporate structure, including merger or dissolution.[188] We also clarify that non-majority or non-voting investors may hold rights of first refusal, provided that right is exercisable only to prevent dilution of the investor's interest or a transfer of control by the control group to a third party. We also observe that we would not look favorably upon an assignment or transfer of a license that resulted from rights of first refusal being exercised if (1) the holder of such rights was a manager of the licensee, and (2) there was evidence the manager had not acted to maximize the profitability

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[185] *See* note 183 *infra.*

[186] *See* GO Communications *ex parte* comments, filed Nov. 3, 1994, at 5-6.

[187] *See, e.g., News International*, 97 FCC 2d 349, 357-66 (1984) (describing minority shareholder voting and consent rights that serve to protect interests and do not constitute a transfer of control); *Data Transmissions*, 44 FCC 2d 935, 936-37 (1974) (same).

[188] Our most recent decision on such voting and consent rights addressed an agreement between MCI Communications Corporation (MCI) and British Telecommunications plc (BT). In that *Order,* we evaluated whether particular voting and consent rights intended to protect BT's investment in MCI triggered a transfer of control. *See Declaratory Ruling and Order*, 9 FCC Rcd 3960 (1994). We indicated that covenants that give a party the power to block certain major transactions of a company do not in and of themselves represent the type of transfer of corporate control envisioned by Section 310(d) of the Communications Act. We found it significant, however, that while BT could block certain major transactions by MCI, BT could not compel MCI to engage in such major transactions. Thus, we concluded that BT's power was permissibly limited to protecting its own investment in MCI. *Id.* 9 FCC Rcd at 3962. *See also McCaw Cellular Communications, Inc.*, 4 FCC Rcd 3784 (Com. Car. Bur. 1989).

of the business in order to ensure that the options would be exercised at a lower price.

82. While we conclude that the provisions described above will generally not be considered to deprive an otherwise qualified control group of *de facto* control, some proposals made by petitioners and commenters to benefit non-majority shareholders would violate this standard. For example, non-majority shareholders should not have the power to select or replace members of the control group or key employees of the corporation. Further, as discussed in the *Second Report and Order* in this docket, we do not intend to restrict the use of preferential dividends and liquidation preferences. We will scrutinize, however, any mechanisms that deprive the control group of the ability to realize a financial benefit proportional to its ownership of the applicant.[189] Finally, we emphasize that any final determination of whether a control group has yielded *de facto* control to outside investors must depend on the circumstances of the particular case. For example, while certain provisions benefitting non-majority investors may not give rise to a transfer of control when considered individually, the aggregate effect of multiple provisions could be sufficient to deprive the control group of *de facto* control, particularly if the terms of such provisions vary from recognized standards.[190] To facilitate review of such provisions, we will amend the Form 401 (long-form)[191] to require winners of C and F block auctions to disclose any such covenants and terms that protect non-majority investors' rights in the licensee.

b. Management Contracts

83. Background. An issue of concern to many petitioners and commenters is whether designated entities may enter into management agreements with third parties without being deemed to have engaged in an unauthorized transfer of control. Although we did not expressly address this issue in the *Fifth Report and Order*, we have traditionally scrutinized common carrier management agreements for this purpose under the *Intermountain Microwave*

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[189] *See Second Report and Order,* 9 FCC Rcd 2348 at ¶ 278.

[190] In assessing whether such provisions vary from recognized standards, the Commission may assess whether the provisions are accepted measures to protect financial interests of noncontrolling investors. *See, e.g.,* discussion *supra* at paragraph 81 and *infra* at paragraphs 94-95; Model Business Corporations Act and Uniform Limited Partnership Act.

[191] FCC Form 600 will replace both Form 401 (used under Part 22 of the Commission's Rules) and Form 574 (used under Part 90 of the Commission's Rules). *Third Report and Order* in Gen. Docket No. 93-252, FCC 94-212 (released September 23, 1994) at ¶ 286. Applicants must use Form 600 beginning January 2, 1995. *Id.* ¶¶ 298, 414. The Commission has received a Motion for Stay of the January 2, 1995 effective date, which is currently pending. National Association of Business and Educational Radio, Inc., *Motion for Partial Stay of the Third Report and Order* in Gen. Docket No. 93-252, filed November 4, 1994.

test,[192] and we recently extended the use of this test to all CMRS providers in our *Fourth Report and Order* in Gen. Docket 93-252.[193] Under this test, a licensee may enter into a management agreement with a third party provided that the licensee retains exclusive responsibility for operation and control of the licensed facilities, as determined by the following six factors: (1) unfettered use of licensed facilities and equipment; (2) day-to-day operation and control; (3) determination of and carrying out of policy decisions; (4) employment, supervision, and dismissal of personnel; (5) payment of financial obligations; and (6) receipt of profits from operation of the licensed facilities.[194]

84. Petitions. In its petition, Pacific Bell contends that the *Intermountain Microwave* test needs to be clarified to eliminate uncertainty about the permissible scope of management agreements.[195] Pacific Bell notes that the D.C. Circuit has recently remanded a case in which the Commission purportedly misapplied the *Intermountain* test and argues that further guidance from the Commission is therefore needed to prevent sham agreements between designated entities and third party managers.[196] Other parties also support the view that the Commission should clarify its standards regarding management contracts, but do not necessarily agree about what standard should be articulated. NABOB, for example, argues that the *Intermountain* test is too rigid and that a more flexible standard should be applied to designated entities who enter into management agreements.[197] Columbia PCS, on the other hand, contends that the Commission should apply a stricter standard by limiting managers to performing discrete functions on a subcontractor basis as opposed to assuming broad

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[192] *See Intermountain Microwave, Inc.*, 24 Rad. Reg. (P&F) 983 (1963) (*Intermountain Microwave*). *See also Memorandum Opinion and Order* in CC Docket No. 90-257 (*La Star Cellular Telephone Company*), FCC 94-299 (adopted Nov. 18, 1994; released ____) (on remand from the D.C. Circuit).

[193] *Fourth Report and Order*, Gen. Docket No. 93-252, FCC 94-270 (released Nov. 18, 1994) ¶ 20. In this order, we also concluded that management contracts could be considered "attributable interests" for purposes of the PCS/cellular/SMR spectrum cap even if they did not confer control under the *Intermountain Microwave* standard. This conclusion applies only for spectrum cap purposes, however, and does not affect our underlying analysis of when a management contract gives rise to an unauthorized transfer of control. *Id.* at ¶ 25.

[194] *Intermountain Microwave*, 24 Rad. Reg. at 984.

[195] Pacific Bell Petition at 9.

[196] *Id.* at 11-12 (*citing Telephone and Data Systems v. FCC*, 19 F.3d 655 (D.C. Cir. 1994), *vacating and remanding La Star Cellular Telephone Co.*, 7 FCC Rcd 3762 (1992)).

[197] NABOB Petition at 7.

responsibility for system management.[198]

85. Decision. As noted above, we have recently held in Gen. Docket 93-252 that the *Intermountain Microwave* standard applies to all CMRS licensees who enter into management contracts. Because we have determined that broadband PCS licensees will be presumptively classified as CMRS providers,[199] we reaffirm the applicability of the *Intermountain* standard here. We disagree with NABOB's view that this standard is not sufficiently flexible to account for the management needs of designated entities. The six *Intermountain* factors provide reasonable benchmarks for ensuring retention of control by the licensee while allowing for full consideration of the circumstances in each case. In the case of designated entity applicants, they will ensure that designated entities participate actively in the day-to-day management of the company while allowing reasonable flexibility to obtain services from outside experts as well. We believe that relaxing the *Intermountain* standard, by contrast, could give rise to sham agreements in which designated entities do not exercise actual control.

86. While we reject the view that scrutiny of management contracts should be relaxed, we also disagree with the view that such contracts should be subject to a stricter standard than we have applied previously. We conclude that limiting managers to discrete "subcontractor" functions, as Columbia PCS proposes, could prevent designated entities from drawing on managers with broad expertise.[200] Moreover, whether a manager undertakes a large number of operational functions is irrelevant to the issue of control so long as ultimate responsibility for those functions resides with the licensee.

3. Attribution Rules

a. Voting Equity

87. Background. The *Fifth Report and Order* provided that an investor may hold a 25 percent passive equity interest in the entrepreneurs' block applicant before its interest is attributable for purposes of our eligibility rules.[201] In addition, the passive equity investment for closely-held companies could include no more than five percent voting equity, while

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[198] Columbia PCS Opposition to Petitions for Reconsideration (Columbia PCS Opposition), filed Sept. 9, 1994, at 5-6.

[199] *See Second Report and Order*, Gen. Docket No. 93-252, 9 FCC Rcd 1411 (1994) at ¶ 119.

[200] *See e.g.* NABOB Petition at 7-8; Pacific Bell Reply Comments (Pacific Bell Reply), filed Sept. 27, 1994, at 1-3; AIDE Opposition to Petitions for Reconsideration (AIDE Opposition), filed Sept. 9, 1994, at 8.

[201] *Fifth Report and Order*, FCC 94-178 at ¶ 158.

publicly-traded companies could include no more than 15 percent voting equity.[202] In a subsequent *Order*, we increased the threshold percentage of non-attributable voting equity from five percent to 15 percent for closely-held companies.[203] Similarly, for the alternative equity option available to women and/or minority principals, the 49.9 percent passive investment could include no more than 15 percent voting equity.

88. Petitions. Petitioners request that the Commission increase the threshold percentage of non-attributable voting equity from 15 percent to an amount ranging from 20 percent to 49 percent.[204] In addition, petitioners request that the Commission clarify whether the existing rules permit nonattributable investors outside of the control group to hold a less than 25 percent or a less than or equal to 25 percent equity interest in the applicant.[205] Also, on reconsideration of our *Order on Reconsideration* (discussed *supra*), parties have debated our decision to raise the voting equity threshold for closely-held applicants from five to 15 percent.[206] AIDE argues that raising the voting level of closely-held applicants is imprudent because it increases the likelihood that big business will control the applicant.[207] AMP disagrees with AIDE that 15 percent voting control would increase the likelihood of shams, because 15 percent is still not a controlling percentage.[208] Rather, AMP argues that increasing the permissible level of voting equity will enable applicants to attract more equity financing, thereby increasing the applicant's likelihood of success.[209]

89. Decision. We amend our attribution rules to raise the voting equity threshold that qualifies an investor as having an attributable interest in an applicant to 25 percent. We will raise the voting equity level for both publicly-traded and closely-held corporations, and will apply the 25 percent threshold for the 25/75 percent equity option available to all

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[202] *Id.* at ¶¶ 158, 163.

[203] *Order on Reconsideration,* FCC 94-217 at ¶ 8-10.

[204] Omnipoint Petition at 10 (20 percent); CTIA Petition at 6 (25 percent); BET Petition at 14-15 (25 percent); Pacific Telecom Cellular, Inc. Petition for Reconsideration, filed Aug. 22, 1994, at 4 (49 percent).

[205] CTIA Petition at 6, n. 9

[206] *See* AIDE Petition for Reconsideration of *Order on Reconsideration* (filed Sept. 21, 1994); AMP Opposition to Petition for Reconsideration of *Order on Reconsideration* (filed Oct. 17, 1994).

[207] *See* AIDE Petition for Reconsideration of *Order on Reconsideration* at 4.

[208] AMP Opposition to Petition for Reconsideration of *Order on Reconsideration* at 3-4.

[209] *Id.* at 4.