FINAL BRIEF

NOT YET SCHEDULED FOR ORAL ARGUMENT

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 15-1330, 15-1331, 15-1332, 15-1333

SNR WIRELESS LICENSECO, LLC and
NORTHSTAR WIRELESS, LLC, *et al.*, *Petitioners - Appellants*,
v.

FEDERAL COMMUNICATIONS COMMISSION and UNITED STATES OF AMERICA, *Respondents - Appellees.*

On Petitions for Review of an Order of the Federal Communications Commission

INITIAL BRIEF OF PHOENIX CENTER FOR ADVANCED LEGAL AND ECONOMIC PUBLIC POLICY STUDIES AS AMICUS CURIAE IN SUPPORT OF PETITIONERS-APPELLANTS

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April 4, 2016

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

The undersigned attorney of record, in accordance with D.C. Cir. R. 28(a)(1), hereby certifies as follows:

A. Parties and Amici

The following parties currently appear before this Court:

- Northstar Wireless, LLC, *Petitioner-Appellant*
- SNR Wireless LicenseCo, LLC, *Petitioner-Appellant*
- Federal Communications Commission, *Respondent-Appellee*
- The United States of America, *Respondent*
- Public Knowledge, *Amicus Curiae for Petitioners-Appellants*

B. Ruling Under Review

The Phoenix Center for Advanced Legal and Economic Public Policy Studies files this brief as *amicus curiae* in support of the Petitioners seeking review of the Federal Communications Commission's Memorandum Opinion and Order captioned *Northstar Wireless, LLC, SNR Wireless LicenseCo, LLC, Applications for New Licenses in the 1695-1710 MHz, and 1755-1780 MHz and 2155-2180 MHz Bands*, 30 FCC Rcd. 8887 (rel. Aug. 18, 2015) ("*Order*"), JA 633.

C. Related Cases

The Phoenix Center is not aware of any other related cases.

s/ *Lawrence J. Spiwak*

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CERTIFICATE OF COUNSEL REGARDING AUTHORITY TO FILE AND SEPARATE BRIEFING

On December 23, 2015, the Phoenix Center filed with this Court its notice that it intends to file a brief of up to 7000 words as amicus curiae in support of the various Petitioners in this case. All Petitioners and Respondents in this case have consented to the filing of this brief. Pursuant to Circuit Rule 29(d), counsel for the Phoenix Center hereby certifies that no other non-government *amicus* brief of which they are aware relates to the subjects addressed herein. Accordingly, the Phoenix Center, through counsel, certifies that filing a joint brief would not be practicable.

s/ *Lawrence J. Spiwak*

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CORPORATE DISCLOSURE STATEMENTS

Pursuant to Federal Rule of Appellate Procedure 26.1 and D.C. Circuit Local Rule 26.1, the Phoenix Center for Advanced Legal & Economic Public Policy Studies submits the following corporate disclosure statement. The Phoenix Center is a non-profit 501(c)(3) non-stock corporation organized under the laws of Maryland. As such, the Phoenix Center has no parent companies and no one holds an ownership interest in the Phoenix Center.

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CERTIFICATE REGARDING AUTHORSHIP

Pursuant to Federal Rule of Appellate Procedure 29(c)(5), the Phoenix Center certifies that no party's counsel authored this brief, in whole or in part; that no party or party's counsel contributed money that was intended to fund preparing or submitting the brief; and that no person other than the Phoenix Center contributed money that was intended to fund preparing or submitting the brief.

s/ *Lawrence J. Spiwak*

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ADMINISTRATIVE MATERIALS:

MISCELLANEOUS:

GLOSSARY:

Auction 97:	The recently concluded auction at issue in the case at bar
AWS:	Advanced Wireless Services
DE:	Designated Entity
FCC:	Federal Communications Commission

INTEREST OF AMICUS CURIAE:

The Phoenix Center is a non-profit 501(c)(3) research organization that studies the law and economics of the digital age. Among other topics of research, the Phoenix Center has written extensively about how the Federal Communications Commission ("FCC") has designed and implemented spectrum auctions. Most recently, the Phoenix Center has studied both the legal and economic underpinnings of the "Designated Entity" ("DE") program at issue in this case. The Phoenix Center has also written extensively about the Commission's practice and procedure, including the Agency's mixed track record in following procedural due process and legal precedent. The Phoenix Center, therefore, has an established interest in the outcome of this proceeding and we believe that our perspective on the issues will assist the Court in resolving this case.

SUMMARY OF ARGUMENT:

Auction 97 was the most financially successful spectrum auction ever administered by the Federal Communications Commission. Winning bids totaled $45 billion for the mid-band AWS-3 spectrum auctioned, exceeding expectations more than two-fold. The U.S. government would ultimately net only $41.2 billion, however, because of $3.6 billion in bidding credits granted to small businesses that applied for DE status. SNR Wireless and Northstar Wireless, the Petitioners in this case, were two of these DEs. The Petitioners entered into agreements with a larger strategic investor, DISH Network Corporation, and modeled these agreements on structures approved by the FCC in past auctions. Petitioners also disclosed these agreements in applications submitted to the FCC prior to the auction. After review, the Commission certified the Petitioners as "Qualified Bidders" and allowed them to participate in the auction as "Designated Entities." The Petitioners offered winning bids totaling $13.3 billion (30% of the auction's proceeds) and received $3.3 billion in bidding credits (92% of total credits for the auction). In terms of the sheer size of the winning bids, Auction 97 was not only the most successful auction in FCC history, but it was also the most successful auction in the history of the DE program.

This case is about one of two things: (a) the legality of the Petitioners' relationship with DISH; or (b) the Federal Communications Commission's disregard of the rule of law and its disrespect for procedural due process when its rules produce an outcome the Agency does not like. We argue it is more the latter.

As we see it, the Petitioners have made a compelling case that they adhered to the rules and relied on FCC precedent. If the Court agrees, then the central issue at bar is whether the FCC should be allowed to alter the rules of Auction 97 *post hoc* after deciding that the results were not to its liking. Just because the Commission had a problem with the auction's results—that is, a $3.3 billion bidding credit due bidders with disclosed financial agreements with DISH—it was not at liberty to disavow its own precedent to shift blame to the Petitioners for the *perceived* shortcomings of the Commission's rules and the Agency's own inaction.

Financial relationships between DEs and larger, well-financed entities were not new to Auction 97. Indeed, the FCC has long-allowed (and in fact encouraged) such relationships over the years, provided that (a) such relationships were fully disclosed in advance; and (b) the winning bidders adhered to strict post-auction rules to prevent "unjust enrichment" by flipping

subsidized spectrum for private gain. Equally as important, prior to Auction 97, the Commission imposed no limit on the size of the bidding credits that a DE could receive. Thus, if the Commission was uncomfortable with the potential of its rules to produce billions in bidding credits, then the onus was on the Agency either (a) to alter its rules prior to Auction 97; or (b) to intervene during the auction the minute it believed the credits were too large. While the Commission did change its rules for future auctions immediately following Auction 97—rule changes that (now unsurprisingly) limit the size of bidding credits, thus revealing the true source of discontent in this matter—it does not alter the fact that the Agency is not at liberty to retroactively apply those rule changes *post hoc*, whether in letter or spirit. Yet, here we argue that the evidence points to the Commission being guilty of exactly this type of mischief. We ask that this Court deem the Commission's actions in the case to be arbitrary and capricious and, in doing so, restore integrity to spectrum auctions and the Commission's rulemaking process.

The facts in this case are straightforward.

First, the FCC established the rules for Auction 97 through public notice and comment. In this public notice, the Commission specifically instructed firms seeking a determination to be a "Designated Entity" (and thus be eligible

for bidding credits) to "review carefully" the well-developed Agency precedent on this matter. It appears that the Petitioners carefully followed precedent in order to satisfy the FCC's rules, borrowing heavily from agreements previously approved by the Commission. While the Agency leaves a formal examination of these agreements until after the auction concludes, the Short Form process nonetheless provides the Commission with ample information about financial arrangements and joint bidding agreements among DEs and their financial backers. Given full and public knowledge of the agreements and DISH's aggressive spectrum acquisition history, if the FCC had concerns about the relationship between the Petitioners and DISH, then the FCC could have easily rejected the Petitioners' respective Short Forms. (Indeed, while the FCC's Short Form process may be perfunctory, it is not *pro forma*.) It did not. Instead, apparently unmoved about the Petitioners' relationship with DISH, the FCC certified the Petitioners as "Qualified Bidders" and allowed them to participate in the auction as "Designated Entities."

Second, the FCC was likewise unimpressed with the impact of the Petitioners' relationships with DISH during the auction. Auction 97 data reveal that the bidding credits had exceeded $3 billion within one week of the

eleven-week auction (Round 23 of 341). Bidding credits would reach nearly $4 billion, almost all of which was attributable to the Petitioners, by the 12th day of bidding. Under the terms of its own auction rules, if the Commission believed that Petitioners were "too successful" in the auction, then the Agency could have intervened at that point. Again, it did not.

Third, after Auction 97 concluded and the size of the bidding credits were publicly revealed, allegations that the Petitioners violated the Commission's rules spread like wildfire around Washington. Only then did the FCC perceive a problem, and that problem was mainly the Commission's embarrassment from media coverage suggesting that the Petitioners had somehow bamboozled the Agency about their relationship with DISH. In response, both Democrat and Republican FCC Commissioners felt the pressure to act. For example, FCC Commissioner Ajit Pai, testifying before the Senate Appropriations Committee, remarked that "[a]llowing DISH to obtain over $3 billion in taxpayer-funded discounts makes a mockery of the small business program." Not to be outdone, FCC Chairman Tom Wheeler testified before Congress that he intended to "fix this" because he was "against slick lawyers coming in and taking advantage of a program that was designed for a specific

audience and a specific purpose" and opposed having "designated entities be beards" for large companies.

A clean "fix" would prove elusive. Within months after Auction 97 concluded, the Agency amended its DE Rules to significantly cap the amount of bidding credits a DE may receive and to ban joint bidding agreements for future auctions, effectively conceding that the undesired outcome of Auction 97 was a logical outgrowth of the rules in place for that auction. Admitting that it cannot apply its rule changes retroactively, the Commission was forced to engage in some legal gymnastics to revoke the Petitioners' bidding credits. Indeed, although the Commission conceded that "the entire record indicates" that the Petitioners complied with the Agency's rules and adhered to precedent, the Commission attempted to get around these inconvenient truths by declaring that the Petitioners "simply proceeded under an incorrect view about how the Commission's affiliation rules apply to these structures" and under the "totality of the circumstances" the Petitioners did not warrant DE classification. But what about the past Commission precedent upon which the Petitioners relied? The Commission—*in a footnote*—simply sweeps this precedent under the rug, noting—*without any explanation*—that "[t]o the extent any prior actions of Commission staff could be read to be inconsistent

with our interpretation of the Commission's rules in this order, those actions are not binding on the Commission—and we hereby expressly disavow them…."

The Commission may not escape responsibility for its choices about running Auction 97 by blaming Petitioners *post hoc* for having an "incorrect view" about their take on the rules (with nearly twenty years of prior Commission interpretation and application) and by disavowing its own precedent without explanation. The Petitioners had every right to rely on Commission precedent—particularly when the Commission specifically instructed them to do so. Moreover, since the Commission chose to postpone the detailed review of the DE applications and agreements until after the auction was complete, the Petitioners had no choice but to rely on precedent. It was the Commission that asked participants to bid billions on spectrum licenses before it offered final confirmation on each bidder's qualifications, so it was the Commission that made precedent so critically important. Abrogating precedent in such an arbitrary and capricious way raises serious issues of procedural due process.

Finally, by moving the goal post after the conclusion of the auction, the Commission has done great damage to the integrity of the auction. The

Petitioners bid in expectation of receiving a 25% discount. With that discount now denied, their bids no longer satisfied the rational calculus upon which they were made and, in bidding on 80% of the available licenses and forcing rival bidders to alter their own strategies, the prices for essentially all the available licenses were impacted by the Petitioners' participation. By declaring post-auction that the Petitioners (both qualified for the auction by the Agency) are ineligible for the bidding credits on which their bidding decisions were made but permitted them to bid anyway, the Commission has put the results of Auction 97—*all of the results*—in doubt.

ARGUMENT:

I. The Rules in Place at the Time of Auction 97 were Expressly Designed to Encourage Large Firm Investment in Designated Entities Via Arms-Length Financial Roles.

A. *Background*

For many years, U.S. spectrum licensing policy was a mess. Using both "beauty pageants" and lotteries, spectrum licensing was extremely inefficient. In the 1990s, spurred on by the work of Nobel Laureate Ronald Coase, the United States moved towards a policy of auctioning spectrum rather than giving it away. *See, e.g.*, T.W. Hazlett, D. Porter, and V.L. Smith, *Radio Spectrum and the Disruptive Clarity of Ronald Coase*, 54 JOURNAL OF LAW AND ECONOMICS 125-166 (2011). The theory supporting this policy was simple and elegant: the firm which values the spectrum most will put the spectrum to its best and most efficient use, with the bonus of revenues for the U.S. Treasury.

That said, Congress was not ready for the total surrender of spectrum license assignment to market forces; the desire to cater to political constituencies was irresistible. So while the Communications Act directs the FCC to auction spectrum via "competitive bidding," the Communications Act also directs the Commission to "disseminat[e] licenses among a wide variety

of applicants, including small businesses, rural telephone companies, and businesses owned by minority groups and women." 47 U.S.C. §309(j)(3)(B). To make sure these constituencies can afford to participate in the auctions against larger, established mobile providers, the statute directs that the Commission shall, among other things, "consider alternative payment schedules and methods of calculations, including lump sums or guaranteed installment payments…." 47 U.S.C. §309(j)(4)(A). In particular, to "ensure that small businesses, rural telephone companies, and businesses owned by minority groups and women are given the opportunity to participate in the provision of spectrum-based services" the Commission shall "consider the use of tax certificates, bidding preferences, and other procedures." 47 U.S.C. §309(j)(4)(D).

Such preferences intentionally put licenses in the hands of entities with lower values for the spectrum than others. Since markets abhor inefficiency, profit seekers are expected to seek ways to reallocate the licenses to higher-valued uses after the auction. *C.f.,* T.R. Beard, G.S. Ford, L.J. Spiwak, and M. Stern, *Taxation by Condition: Spectrum Repurposing at the FCC and the Prolonging of Spectrum Exhaust,* PHOENIX CENTER POLICY PAPER NO. 44 (September 2012). A rule that promotes inefficiency requires additional rules

to impede nature's desire to purge the inefficiency. Recognizing the incentives created by this subsidy to favored groups, Congress also requires the Commission to promulgate "transfer disclosures and anti-trafficking restrictions and payment schedules as may be necessary to prevent unjust enrichment as a result of the methods employed to issue licenses and permits." 47 U.S.C. §309(j)(4)(E). For the better part of the last twenty years, the FCC has struggled to find the appropriate balance of promoting Congress's twin goals of establishing spectrum preferences for small businesses and protecting against "unjust enrichment." *See, e.g., Fresno Mobile Radio, Inc. v. FCC*, 165 F.3d 965, 971 (D.C. Cir. 1999) (when it comes to spectrum policy, the FCC "must balance a number of potentially conflicting objectives"); *accord*, *Rural Cellular Ass'n v. FCC*, 588 F.3d 1095, 1103 (D.C. Cir. 2009).

While a detailed exegesis of the Commission's DE rules would take far too long for this brief, to help educate this Court we present a concise overview of the rules which applied to Auction 97. To begin, the FCC set up a schedule of potentially-available bidding credits based upon the revenue of the DE along the following lines:

- Businesses with average gross revenues for the preceding three years not exceeding $15 million are eligible for bidding credits of 25% of the license purchase price; and

- Businesses with average gross revenues for the preceding three years not exceeding $40 million are eligible for bidding credits of 15% of the license purchase price. 47 C.F.R. §1.2110 (f)(1)-(2).

Recognizing that these large discounts are enticing for larger players, the FCC's rules include two mechanisms to discourage the abuse of the DE program and prevent "unjust enrichment."

First, under its attribution rules, the Commission looks to determine whether an individual or entity with revenues in excess of the DE program's thresholds has either *de jure* or *de facto* control of a DE. Identifying *de jure* control is relatively easy, as the Commission looks to see if somebody holds over 50% of voting stock or a partnership interest. Determining *de facto* control is a bit more challenging. To do so, the Commission looks on a case-by-case basis at the following factors: (1) Does an investor control more than 50% of the board of directors or management committee of the DE? (2) Does an investor have the authority to appoint, promote, demote and fire senior executives that control the day-to-day activities of the licensee? And (3) does the investor play an integral role in management decisions? 47 C.F.R. §1.2110(b)(iii). These requirements have applied to numerous spectrum auctions prior to Auction 97, so substantial precedent exists on the Commission's interpretation and application of its rules.

Second, the FCC's rules include mechanisms to prevent a DE from purchasing spectrum at a discount and then immediately "flipping" it at a hefty profit. To deal with the problem of "unjust enrichment," the FCC's primary mechanism of enforcement for Auction 97 was a five-year holding rule from which everything else flowed. For example, if a DE violates the Commission's extensive financial attribution rules within five years, then it must then pay back all or a portion of its bidding credits. Similarly, if a DE sells its spectrum to a non-DE before the end of the five-year holding period, then it must repay all or a portion of its bidding credits. Moreover, the rules required DEs at some point to build a network and to become facilities-based providers.[1] *See CSEA/Part 1 Second Report and Order* at ¶ 21. Finally, under the rules governing Auction 97, if a DE leases or resells (including under a wholesale agreement) more than 25% of the spectrum capacity of any one of its licenses to the same person or party, then that DE enters into an "attributable material relationship" ("AMR") and the DE must repay all or a

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[1] Shortly after Auction 97 concluded, the Commission eliminated the facilities-based investment requirement. *See 2015 DE Rules* (JA at 456 *et seq.*)

portion of its bidding credits if those additional attributed revenues cause the DE to exceed the DE revenue limits.[2] 47 C.F.R. §1.2110(b)(iv).

In full recognition of the incentives created by the preferential treatment of favored constituencies in an auction, these are the rules the FCC crafted. If a party adheres to the Agency's attribution and unjust enrichment rules and accepts the consequences of departing from them, then that party should expect to receive bidding credits that reduce the cost of licenses won at auction. As to the success of a DE in the auction, the Commission may very well have expected that its attribution and unjust enrichment rules were sufficient to preclude a DE from winning billions in spectrum licenses in Auction 97. (Again, under the rules in place for Auction 97, there were no caps on the amount of bidding credits a DE may receive.) Thus, it was the Commission—not the Petitioners—that "proceeded under an incorrect view" about how the Auction 97 rules were supposed to function. *Order* at ¶ 132 (JA at 687). Nothing in the rules for Auction 97 *prohibited* the considerable success of a DE at auction; all that was required was an entity willing to take

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[2] Similar to its elimination of the facilities-based entry requirement, shortly after Auction 97 concluded, the Commission also eliminated the AMR Rule. *2015 DE Rules, id.*

on the considerable financial risk—resulting from the lack of either *de facto* or *de jure* meaningful control mandated by both the Commission's attribution and unjust enrichment rules—of backing a DE winning billions in licenses. It is, after all, the DE and not the backer that obtains the licenses (at least for a 5-year post-auction window). Indeed, the fact the rules of Auction 97 did not prohibit such an outcome is demonstrated no more plainly than in the FCC's significant revision of its DE Rules shortly after Auction 97 concluded in July 2015 to limit a DE to $25 million in bidding credits for each eligible small business. *2015 DE Rules* at ¶ 115 (JA at 504).

B. *Prior to Auction 97, the Commission Actively Encouraged DE Partnerships with Established Players So Long as Those Relationships Were Fully Disclosed*

When viewed objectively, the DE Program presents a bit of a conundrum: on the one hand, DE qualification is based upon revenues (or, more accurately, *the lack thereof*). On the other hand, spectrum is expensive, so DEs need access to significant capital if they are to participate meaningfully in any

auction. But where does this capital come from? In general, the answer is other well-financed players.[3]

If the Commission really wanted to avoid having Designated Entities act as (to use FCC Chairman Tom Wheeler's word) "beards" for large companies,[4] then the Agency could have simply prohibited DEs from having *any* financial relationship with a large business, either before or after the auction, and prohibit any license transfer or spectrum leases to a business that does not qualify as a DE. In fact, over the years the Commission has

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[3] The Court should take note of the NextWave debacle from the 1990s, where a DE was forced to forfeit its spectrum because it could not afford to pay for its winning licenses even with the advantage of significant bidding credits. *See, e.g.*, D. Porter and V. Smith, *FCC License Auction Design: A 12-Year Experiment*, 3 J.L. ECON. & POLICY 63 (2007) at fn. 20 ("The C block auction, completed in May 1996, extended bidding credits to Designated Entities (DEs), small businesses or rural telephone companies determined by the FCC to be handicapped in accessing credit markets. DE bidders winning licenses were extended long-term (10-year) credit on extremely favorable terms (U.S. Treasury debt interest rates), paying for licenses via installments. The two largest bidders defaulted on their payments, leading to court battles resolved by the U.S. Supreme Court in 2003."); *see also* NextWave Wireless, WIKIPEDIA (available at: http://en.wikipedia.org/wiki/NextWave_Wireless).

[4] R., Knutson, *FCC to Tighten Reins on Wireless Licenses*, WALL STREET JOURNAL (March 18, 2015); J. Eggerton, *Wheeler: We Will Fix Auction DE Rules*, BROADCASTING & CABLE (March 18, 2015).

considered a prohibition on financial relationships between DEs and "a large in-region incumbent wireless service provider" or "a large entity that has a significant interest in communications services." *See, e.g., CSEA/Part 1 Second Report and Order* at ¶ 2. To date, the Commission has rejected such an outright prohibition. *See, e.g., 2015 DE Rules* (JA at 456 *et seq.*). If anything, the Agency's precedent and policies leading up to Auction 97 *encouraged* DEs to partner with established players *so long as those relationships are fully disclosed*.[5] As stated by the FCC in its *CSEA/Part 1 Second Report and Order*, "*… it is the agreement, as opposed to the party*

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[5] Under the Commission's rules, prospective bidders must "identify on their short-form applications any parties with whom they have entered into any consortium arrangements, joint ventures, partnerships or other agreements or understandings which relate in any way to the competitive bidding process. Bidders will also be required to certify on their short-form applications that they have not entered into any explicit or implicit agreements, arrangements or understandings of any kind with any parties, other than those identified, regarding the amount of their bid, bidding strategies or the particular properties on which they will or will not bid." In the Commission's view, such disclosure requirements will both "deter bidders from engaging in anticompetitive behavior" and "facilitate the identification and investigation of any suspect bidding behavior." *1994 Anti-Collusion Order* at ¶ 225; *see also* 47 C.F.R. § 1.2105(a)(v)(iii) (prospective bidders must certify "as truthful under penalty of perjury, identifying all parties with whom the applicant has entered into partnerships, joint ventures, consortia or other agreements, arrangements or understandings of any kind relating to the licenses being auctioned, including any such agreements relating to the post-auction market structure.")

with whom it is entered into, that causes the relationship to be ripe for abuse …." *Id.* at ¶ 23. As the Commission clearly explained, its approach was to implement safeguards that are effective irrespective of the parties involved rather than focus on the identities of the parties to an agreement.

In crafting the DE rules, the Agency made a strategic choice, balancing the risk of large-firm involvement with the need for capital. Accordingly, there is significant FCC precedent for major wireless carriers investing in DEs. Below are just four examples:

- In Auction 35 (2001), Cingular Wireless, the second largest mobile wireless provider at the time, paid $285 million for an 85% stake in a DE called Salmon PCS. Salmon won 79 licenses (many in major metropolitan areas) at a cost of $2.3 billion. *Seventh CMRS Report* at p. C-9. According to FCC records, Salmon received nearly $560 million (approximately 25%) in bidding credits as a DE. *Auction 35 Results.*

- Also in Auction 35, AT&T Wireless, the third largest mobile wireless provider at the time, secured approval to hold up to 79.4% in a DE named Alaska Native Wireless ("ANW"). *Seventh CMRS Report.* ANW won 44 licenses, some with bidding credits and some licenses that were "closed" to bidding by non-DEs, at gross winning bids totaling $2,960,258,000, with bidding credits of $67 million. *Auction 35 Results*.

- In Auction 58 (2005), Verizon (the second largest mobile wireless operator at the time) obtained an 85% interest in a DE called Vista PCS. (*Eleventh CMRS Report* at p. 102.) Unlike most other auctions, Auction 58 contained both "open" licenses (which could be bid on by any bidder in the auction) and "closed" licenses (which

could only be bid on by certain DEs). *September 2004 Public Notice.* In Auction 58, Vista won 37 closed licenses in major cities such as Houston, Seattle and Pittsburg without having to bid against major carriers. *February 2005 Public Notice.*

- In Auction 66 (2006), Leap Wireless ($2.23 billion in annual revenues) had an 85% interest in a DE called Denali Spectrum. *Twelfth CMRS Report* at p. 132. Denali won licenses in major markets such as Chicago, Minneapolis, and Milwaukee. According to FCC records, Denali's total gross bids in Auction 66 were $365,445,000, with bidding credits of approximately $91 million. *Auction 66 Final Results*.

As Petitioners explain in their brief, the Agreements at issue in this case were closely modeled upon the agreements previously sanctioned by the Commission in these examples. Petitioners Brief, *passim*. Accordingly, for the Commission to reject the arrangements at issue in this case after Auction 97 concluded because of FCC Chairman Tom Wheeler's sudden revelation that "slick lawyers" somehow took "advantage of a program that was designed for a specific audience and a specific purpose" simply does not hold water. WALL STREET JOURNAL, *FCC to Tighten Reins.* Precedent matters, and the Commission is not free to callously disregard it whenever the Agency finds it politically expedient to do so.

II. The Commission Could Have Stopped Auction 97 at Any Time but Deliberately Chose Not To

A. *The Commission Could Have Rejected Petitioners as Qualified Bidders Based on the Short Form Application*

Prior to Auction 97, the Commission required interested bidders to file a "Short Form" application and disclose the identity and relationships of those persons or entities that directly own or control the applicant. *See* 47 C.F.R. §§ 1.2112, 1.2105. At that point, the Commission and all bidders are fully aware of the identity of the firms involved and the nature of their financial relationships. Based on that information, the Agency has the authority to grant or deny both DE status and "Qualified Bidder" status.

In the case at bar, the Commission specifically instructed potential bidders seeking DE status to "… review carefully the Commission's decisions regarding the designated entity provisions." *July 2014 Public Notice* at ¶ 79 (JA at 26). The Petitioners did so, and both fully disclosed their relationship as well as provided detailed summaries of their agreements with DISH in their Short Form application (Petitioners' Brief at 16), basing their agreements directly upon agreements the Commission previously found to be acceptable. *Id., passim*. As the Commission concedes in the *Order* on appeal, "the entire record indicates" that the Petitioners complied with the Agency's rules and

properly disclosed their ownership structure and related Agreements as required. *Order* at ¶ 132 (JA at 687). Accordingly, the Commission found no objection with these investments and both certified the Petitioners as "Qualified Bidders" and allowed the Petitioners to participate in the auction as "Designated Entities." *October 2014 Public Notice*. If the FCC had a problem with the relationship between the Petitioners and DISH, then the FCC could have rejected the Petitioners' Short Form. It did not.

While the FCC's Short Form process may be perfunctory, it is not *pro forma*.[6] After all, it strains credulity to think that the Agency would allow an entity who publicly discloses detailed financial relationships with two other bidders—including the use of joint bidding agreements—to participate in a federal spectrum auction based on a mere "rubber stamp." If so, then the competency of the Agency to run an auction with billion at stake is in doubt.

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[6] *See July 2014 Public Notice* at D-15 (JA at 87) ("After the deadline for filing short-form applications, the Commission will process all timely-submitted applications to determine which are complete, and subsequently will issue a public notice identifying (1) those that are complete, (2) those that are rejected, and (3) those that are incomplete or deficient because of minor defects that may be corrected. Once that public notice is released, any interested parties may be able to view the short-form applications by searching for them in the Commission's database.")

Along a similar vein, in light of the open disclosures in the Petitioners' Short Form application, one has to wonder exactly what the Commission was thinking about the Petitioners and DISH. Anyone with even a passing knowledge of the mobile wireless industry was aware that DISH was on a spectrum buying spree. In 2014, DISH acquired at auction the 10 MHz H Block (1,915-1,920; 1,995-2,000) for $1.56 billion. T. Ream, *Dish Network Sweeps H-Block Spectrum Auction For $1.56 Billion*, FORBES (March 5, 2015). In 2013, DISH made a run to acquire Sprint. (*Id.*) In 2011, DISH purchased 40 MHz of MSS spectrum in the 2 GHz band ("AWS-4 band") for $3 billion. DISH was obviously intending to be a player in Auction 97. In light of the pre-auction disclosures, the Agency's long and tortured experience with the DE Program (*see* S. Labaton and S. Romero, *FCC Auction Hit with Claim of Unfair Bids*, NEW YORK TIMES (February 12, 2001)), and DISH's reputation as a spectrum buyer, the Commission—as the purported "expert" agency—cannot credibly claim that it was ignorant of the possibilities before the auction began.

B. *Auction 97 Data Reveal that the Commission Knew Within Seven (7) Days that Bidding Credits Exceeded $3 Billion Threshold Yet Did Nothing to Stop the Auction*

The Commission also cannot claim ignorance of potential problems once Auction 97 got under way. The Auction 97 data make clear that bidding credits crossed the $3 billion threshold in round 23 (of 341), which occurred only 7 days into the 76 day auction. Moreover, credits nearly reached $4 billion by the 12th day of bidding, with almost all of those credits going to the Petitioners. The FCC unquestionably knew early in the auction that the Petitioners had run up billions in bidding credits. G.S. Ford and M. Stern, PHOENIX CENTER POLICY PERSPECTIVE NO. 15-04: *Ugly is Only Skin Deep: An Analysis of the DE Program in Auction 97* (July 20, 2015). Under the plain terms of the rules for Auction 97, the agency by "public notice or by announcement during the auction [can] delay, suspend, or cancel the auction in the event of natural disaster, technical obstacle, administrative or weather necessity, evidence of an auction security breach or unlawful bidding activity, *or for any other reason that affects the fair and efficient conduct of competitive bidding*." *July 2014 Public Notice* at ¶ 180 (JA at 52) (emphasis supplied). If the FCC had a problem with the Petitioners' relationship with DISH and the size of the bidding credits accrued, then it was at this point the

Commission should have acted rather than delay action until the omelet was scrambled.

Yet, despite direct knowledge of both the size of the bidding credits (within the first week) and, equally as important, the parties eligible for such bidding credits, *the FCC again opted to do nothing*. Instead, the Commission let Auction 97 proceed without intervention for a total of 341 rounds. It was only after the winners of the auction and the size of the bidding credits were publicly announced—and followed by media attention—did the FCC feel politically pressured to act.[7] *See* WALL STREET JOURNAL, *FCC to Tighten Reins.*

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[7] There is even a more cynical interpretation for the Commission's failure to act during the auction: DE participation increases the competitiveness of the auction and thereby drives up prices. (Ford and Stern, *Ugly is Only Skin Deep*.) Given the Petitioners aggressive and widespread bidding, their influence on auction prices was considerable. By allowing the auction to proceed, despite being fully aware of the magnitude of the bidding credits within the first week of bidding, the Commission's inaction, and post-auction denial of the Petitioners' bidding credits, may be viewed as an attempt at auction manipulation by the Commission (the auctioneer). Without dispute, had the auction ceased and the Petitioners' bidding credits brought under scrutiny and denied, then total auction proceeds would have been lower. Faced with interfering with the most successful auction in its history, the Commission let the auction play out, using the Petitioners as shill bidders. Whether or not such an accusation has any merit requires more information

C. *Allowing Petitioners to Bid as "Designated Entities" Impacted the Entire Auction. If the Court Upholds the Commission in this Case, then the Entire AWS-3 Auction Must be Re-Held*

By certifying the Petitioners as "Qualified Bidders" and allowing them to participate in Auction 97 as "Designated Entities", the Petitioners' bidding behavior (i.e., bidding on the assumption of a 25% discount) affected the prices of all licenses in Auction 97, not just those licenses that the Petitioners won. Indeed, the Petitioners' involvement in Auction 97 was pervasive, affecting prices for licenses they won, they lost, and even those they did not bid on. By declaring post-auction that the Petitioners (both qualified for the auction by the Agency) are ineligible for the bidding credits on which their bidding decisions were made but permitted them to bid anyway, the Commission has put the results of Auction 97—*all of the results*—in doubt. Ford and Stern, *Ugly is Only Skin Deep*. As such, if this Court upholds the Agency's decision, then there is a very strong case for this Court to require the Commission to re-stage the auction (the consequence of which is likely to cost the U.S. Treasury far more than $3 billion and tarnish the Commission's reputation as a competent auctioneer and regulator.) R. Kaminski, *FCC to*

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than is publicly available, but the public data is certainly consistent with the hypothesis.

Deny DISH Subsidies: What's Next?, CAPITAL ALPHA PARTNERS (July 17, 2015) ("we expect any re-auctioned licenses to sell for lower prices.").

III. The Commission Cannot Move The Goal Posts Post-Auction Simply Because They Did Not Like the Results

A. *Putting the Size of the Bidding Credits Into Context*

While $3.6 billion is a large number, the large value of the bidding credits is not particularly surprising for a $45 billion auction. Across the FCC's spectrum auctions held prior to Auction 97, the average difference between gross and net bids is 14.5% and the median difference is 13%. The range is 0% to 36%. For a $45 billion auction, therefore, the expected bidding credit is around $6 billion, which is nearly twice the total credit from Auction 97. While $3.6 billion is certainly a lot of money, it is a big number in the company of even bigger numbers. By historical standards, the taxpayer got off relatively cheaply in Auction 97. The bidding credits summed to only 8% in that auction, well below the average 14% share. Ford and Stern, *Ugly is Only Skin Deep*.

B. *Political Embarrassment does not Permit the Commission to Violate Due Process*

While the size of the bidding credits should make no difference to this Court in evaluating the legal questions before it, size maters in politics.

Indeed, notwithstanding the economic reality of the results of Auction 97, the sheer size of the bidding credits became a *cause célèbre* on Capitol Hill and shortly after Auction 97 concluded allegations began to swirl that that the Petitioners had somehow bamboozled the Agency about their relationship with DISH. *See, e.g.*, S. Solomon, *How Loopholes Turned DISH into a "Very Small Business"*, NEW YORK TIMES (February 24, 2015) ("Through sleight of hand and aggressive use of partners and loopholes, DISH turned itself into that very small business, distorting reality and creating an unfair advantage.") In response, both Democrat and Republican FCC Commissioners felt the pressure to act. On the Republican side, FCC Commissioner Ajit Pai, testifying before the Senate Appropriations Committee, remarked that "[a]llowing DISH to obtain over $3 billion in taxpayer-funded discounts makes a mockery of the small business program." *Statement of Ajit Pai, Commissioner, Federal Communications Commission, Hearing Before the Senate Appropriations Subcommittee on Financial Services and General Government* (May 12, 2015). Not to be outdone, FCC Chairman Tom Wheeler testified before Congress that he intended to "fix this" because he was "against slick lawyers coming in and taking advantage of a program that was designed for a specific audience and a specific purpose" and opposed

having "designated entities be beards" for large companies. WALL STREET JOURNAL, *FCC to Tighten Reins.* But how?

Under established Supreme Court precedent, an administrative agency is free to change policy direction so long as it provides a reasoned explanation. *Fox Television v. FCC,* 556 U.S. 502 (2009). To this end, given its dissatisfaction with the with results of Auction 97, less than six months after Auction 97 closed the Commission did exactly that by modifying its DE rules to cap bidding credits and eliminate joint bidding agreements for future auctions. *See 2015 DE Rules*, *supra* (JA at 456 *et seq.*). However, by its own admission, the Commission could not apply these rule changes retroactively to the Petitioners, who are governed by the rules in place for Auction 97. *Order* at fn. 5 (JA at 634) ("Because Auction 97 took place under our prior rules, our consideration and analysis herein is undertaken under the rules that were in place at the time that the Applicants submitted their respective Form 175 Short-Form Applications ("Form 175 Short-Form Applications") and Form 601 "long-form" Applications…"); *c.f., Bowen v. Georgetown University Hospital*, 488 U.S. 204 (1988) (statutory grants of rulemaking authority will not be understood to encompass the power to promulgate retroactive rules unless that power is conveyed by express terms by Congress).

To escape from this legal pickle, the Commission engaged in some legal gymnastics by both moving the goal posts and then blaming the Petitioners for not understanding the rules of the game.

In particular, the Commission concedes in the *Order* on appeal that "the entire record indicates" that the Petitioners complied with the Agency's rules and properly disclosed their ownership structure and related Agreements as required. *Order* at ¶ 132 (JA at 687). (In fact, the Commission also concedes that "had the Applicants disclosed more detail about what they intended to accomplish through joint bidding with DISH, such disclosure might have communicated bidding strategies to other applicants in violation of the prohibited communications rule…." *Order* at fn 384 (JA at 688).) To get around this inconvenient truth, the Commission pivots and claims that the Petitioners simply "proceeded under an incorrect view about how the Commission's affiliation rules apply to these structures" (*Order* at ¶ 132; JA at 687) and, under the "totality of the circumstances" (*Order* at ¶ 49; JA at 655), the Petitioners did not warrant DE classification.

But what about the past Commission precedent upon which the Petitioners relied? The Commission *in a footnote* simply sweeps this precedent under the rug, noting *without any explanation* that "[t]o the extent any prior actions of

Commission staff could be read to be inconsistent with our interpretation of the Commission's rules in this order, those actions are not binding on the Commission—and we hereby expressly disavow them…." The Petitioners had every right to rely on Commission precedent—particularly when the Commission specifically instructed them to do so and postponed careful review of the applications until after the auction was completed. *July 2014 Public Notice* at ¶ 79 (JA 26) ("… applicants should review carefully the Commission's decisions regarding the designated entity provisions."). Accordingly, the Commission may not escape responsibility for incompetently running Auction 97 by blaming Petitioners *post hoc* for having an "incorrect view" about nearly twenty years of prior Commission behavior.

C. *FCC's Conduct in Auction 97 has Deleterious Effect on Success of Future Auctions, the DE Program, and Broadband Investment Generally*

In light of the evidence, at the core of this case is the credibility of the FCC to adhere to the rule of law and to protect procedural due process, and this is true whether or not SNR and Northstar are disqualified from the bidding credits due to some real or fictional technicality. Of all the myriad ways that regulation can fail, the lack of credibility of the regulator—its inability to keep its word and follow its own precedent—is perhaps the most important.

Participating in the provision of communications services requires large fixed and sunk investments whose returns are realized only sporadically over long periods. If firms and investors fear expropriation of returns by a regulator unable to commit to its policies, then investment will be severely curtailed. *See* G.S. Ford, *Is the FCC's Regulatory Revival Deterring Infrastructure Investment?* BLOOMBERG BNA (November 13, 2015). As noted by Levy and Spiller,

> The combination of significant investments in durable, specific assets with the high level of politicization of utilities has the following result: utilities are highly vulnerable to administrative expropriation of their vast quasi-rents. Administrative expropriation may take several forms. Although the easiest form of administrative expropriation is the setting of prices below long-run average costs, it may also take the form of specific requirements concerning investment, equipment purchases, or labor contract conditions that extract the company's quasi-rents. Where the threat of administrative expropriation is great, private investors will limit their exposure.[8]

Given the Commission's mandate in Section 706 of the Telecommunications Act of 1996 (47 U.S.C. § 1302) to "encourage the deployment on a reasonable

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[8] B. Levy and P. Spiller, The Institutional Foundations of Regulatory Commitment: A Comparative Analysis of Telecommunications Regulation, 10 JOURNAL OF LAW, ECONOMICS, & ORGANIZATION, 201-246 (1994).

and timely basis of advanced telecommunications capability to all Americans," we encourage this Court to hold the FCC accountable for its actions to preserve the public's confidence in the institution.[9]

The FCC's credibility is particularly important in the context of spectrum auctions. If DEs believe that their discounts will be honored only if the Commission likes the outcome of an auction, then they and their partners will be discouraged from future participation. As FCC Commissioner Mignon Clyburn observed in her concurring statement to the *Order* on appeal, the Commission's conduct in this case may have "a chilling effect on the ability of small businesses to enter into relationships with large investors." *Order* at p. 144 (JA at 700). By the same token, if unsubsidized bidders are wary of the Agency's commitment to any part of the auction's rules, then they likewise will reduce their valuations of spectrum licenses and auction revenues will

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[9] The agency's credibility is already is doubt. *See, e.g.,* T.R. Beard, G.S. Ford, L.J. Spiwak and M. Stern, *Eroding the Rule of Law: Regulation as Cooperative Bargaining at the FCC*, PHOENIX CENTER POLICY PAPER NO. 49 (October 2015); G.S. Ford, L.J. Spiwak and M. Stern, *The Broadband Credibility Gap*, 19 COMMLAW CONSPECTUS 75 (2010); L.J. Spiwak, *The FCC's New Municipal Broadband Preemption Order Is Too Clever By Half*, BLOOMBERG BNA (April 10, 2015); G.S. Ford and L.J. Spiwak, *The Unpredictable FCC: Politicizing Communications Policy and its Threat to Broadband Investment*, BLOOMBERG BNA (October 30, 2014).

decline. Even non-DE participants will be squeamish about entering an auction fearing perhaps that the FCC will use the DEs as shill bidders to drive up prices, only later to revoke DE status without any adjustment in final bids to reflect the influence of high bids motivated by bidding credits. While the present controversy is in the auction sphere, the assessment of the credibility of the FCC on this matter reaches well beyond auctions. If investors feel that the Commission will not honor its commitments if it doesn't like the outcome of its policies, then capital will find greener grass. Ford and Stern, *Ugly is Only Skin Deep*.

D. *The Onus Was on the Commission to Pro-Actively Enforce its Rules*

While this case has spurned quite a bit of acrimony around Washington due to the Petitioners' use of the DE program to receive bidding credits, the appropriate focus of this anger should be directed towards the root cause of the problem: Congress and the FCC. Indeed, any time Congress and the Commission set up a subsidy program designed to favor one or more political constituencies, it would be highly naïve for anyone to think that profit-maximizing firms will not also seek to avail themselves of those benefits within the full extent of the law. (Indeed, firms are not passive recipients of regulation.) We have seen firms engage in such conduct for decades with the

FCC's Universal Service and intercarrier compensation paradigms, and the Commission's DE program is no exception. As Steven Solomon recently wrote in the NEW YORK TIMES, aggressive use of the Commission's DE rules "is not a new issue. The 'small firm' exception has been known to be a problem at the FCC for years."[10] *See* Solomon, *supra*. Accordingly, if, as the Commission concedes, the Petitioners complied with the FCC's rules, coupled by the fact that the FCC repeatedly failed to take any action until it was faced with negative media attention *after* Auction 97 had concluded, then this Court should view the AWS-3 auction as a "teachable moment" about the nature of regulation in general—that is, the rules matter, the intentions do not. L.J. Spiwak, *How the AWS Auction Provides a Teachable Moment on the Nature of Regulation*, BLOOMBERG BNA (April 28, 2015). For this reason, the onus

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[10] Indeed, in a paper authored by the Congressional Budget Office in 2005, the CBO specifically found that "the preferences adopted by the FCC in the PCS auctions, particularly those used in the auction for the first large block of spectrum set aside for small businesses, the C block, did not ultimately result in widespread or long-term participation by small businesses in the PCS market. As of 2005, it was a common occurrence that control of a large portion of the PCS spectrum authorized by licenses set aside for small businesses had been sold to large providers; thus, many of the expected benefits of small-business participation were not realized." *Small Bidders in License Auctions for Wireless Personal Communications Services*, CONGRESSIONAL BUDGET OFFICE (October 2005) at p. 1.

should not be on the Petitioners for using "slick lawyers" but upon the government to write better rules and to account—to the extent practicable—for the "law of unintended consequences" when firms interpret rules based upon established precedent. Attempting to "fix this" *post hoc* by moving the goal posts eviscerates procedural due process and reduces the public's trust in government institutions.

CONCLUSION:

The credibility of a regulator comes from its respect of its own rules. Change is permitted, but only on a going-forward basis. How this Court rules on the Commission's behavior in Auction 97 will say much about the future of the Commission's credibility as a regulator and its capacity to run a valid auction. Accordingly, for the reasons set forth herein, the Phoenix Center joins the Petitioners in urging this Court to find unlawful and, therefore, to vacate the Commission's *Order*.

Respectfully submitted,

s/ *Lawrence J. Spiwak*

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Dated: April 4, 2016

CERTIFICATE OF COMPLIANCE:

Pursuant to Federal Rule of Appellate Procedure 32(a)(7)(C) and D.C. Circuit Rule 32(e), the undersigned certifies that this brief complies with the applicable type-volume limitations. This brief was prepared using a proportionally spaced type (TIMES NEW ROMAN, 14 point). Exclusive of the portions exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii) and D.C. Circuit Rule 32(e)(1), this brief contains 6,906 words. This certificate was prepared in reliance on the word-count function of the word-processing system (Microsoft Word 2016) used to prepare this brief.

/s/ *Lawrence J. Spiwak*

Lawrence J. Spiwak
April 4, 2016

CERTIFICATE OF SERVICE:

I hereby certify that, on April 4, 2016, I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the District of Columbia Circuit using the appellate CM/ECF system. Participants in the case who are registered CM/ECF users will be served by the appellate CM/ECF system.

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