



« Back | Print

Guarding The Beachfront

Public Interest Groups Want Cable, Telephone Companies Kept Out of Auction of High-Quality Wireless Spectrum

By Ted Hearn -- Multichannel News, 6/18/2007

Washington— If a handful of public-interest advocates had their way, the Federal Communications Commission would ban cable operators and phone companies from the upcoming 700-MHz spectrum auction that some consider the most important the agency will ever conduct.

Consumers Union, Public Knowledge and the Media Access Project (MAP) are leading the assault, claiming a ban would spur competition in providing high-speed Internet access to consumers. Otherwise, big cable-system operators such as Comcast and Time Warner Cable and phone giants such as AT&T and Verizon Communications would keep out smaller rivals, dominating the business and stifling innovation.

"We think it makes excellent sense just to keep the incumbents out of this auction," said MAP senior vice president Harold Feld. "If we really want a genuine third pipe — that is to say, one that competes against telephone [digital subscriber line] and the cable broadband platform — keep those guys out."

While not unprecedented, sweeping auction restrictions on cable would be a setback as cable operators continue to search for ways to add a robust wireless component to their voice, video and data services. That "triple play" has been such a huge success that it probably led Rupert Murdoch to give up News Corp.'s controlling stake in DirecTV, the leading satellite TV provider.

BEACHFRONT BONANZA

Last year, top cable companies participated in an auction of Advanced Wireless Services spectrum, through an alliance with Sprint called SpectrumCo. Cable-operator participants included Comcast, Time Warner Cable, Cox Wireless, and Bright House Networks. The companies paid \$2.4 billion for 137 licenses, all told.

SpectrumCo hasn't moved rapidly to exploit its AWS holdings, causing MAP's Feld to assert that the cable-led group's plan is to hoard spectrum, blunting competition from possible rivals in providing Internet access. The National Cable & Telecommunications Association has told the FCC that a warehousing strategy would be a waste of resources that cable's lenders and investors would condemn.

This year's auction puts on the block a more highly valued prize. The 700-MHz band — predominantly used today by UHF TV stations that must vacate the space in February 2009 as part of the digital-TV transition — is considered beachfront property. Signals in the 700-MHz band can travel dozens of miles at low power, easily penetrating foliage and solid structures that wireless services operating at higher frequencies can only hope to match.

The favorable propagation characteristics of 700-MHz signals have the potential of saving cable, telephone and other companies billions of dollars in construction and operational expenses, while reducing consumer annoyance with dropped calls at the same time. Some hope the broad geographic range of 700-MHz signals will mean that rural areas receive an affordable broadband alternative to satellite-delivered service.

"It's really the best and it will be the only spectrum of this quality that will be available for a very long time," said Stanford Business School professor Robert Wilson, an auction design expert.

In recognition that an outright cable-telco ban might be politically impossible, public-interest groups are backing various conditions proposed by a coalition that includes Google, DirecTV and EchoStar Communications. FCC adoption of some or all of these proposals could so tilt the game that cable operators could end up sitting out the pricey bidding war altogether.

But the effective exclusion of cable and phone companies owing to biased rules would run the risk of undermining the effort to raise the \$10 billion that Congress is counting on from the 700 MHz auction.

Google's Washington telecom counsel, Rick Whitt, said his company wants the FCC to do whatever it can to promote new entrants in the wireless market. The FCC could do this, he said, by partitioning the spectrum into large 22-MHz blocks that cover multi-state regions.

That would produce the necessary scale to vie with national wireless services offered by AT&T and Verizon Wireless. Direc TV and EchoStar have also endorsed auction rules that facilitate national licensing in the 700-MHz band.

C and F Block Broadband PCS	Ended: 1/26/2001	\$16.8 billion (*)
Advanced Wireless Services (AWS-1)	Ended: 9/18/2006	\$13.7 billion
Broadband PCS C Block	Ended: 5/6/1996	\$10 billion (**)
Broadband PCS A and B Block	Ended: 3/13/1995	\$7.0 billion
Broadband PCS D, E, & F Block	Ended: 1/14/1997	\$2.5 billion
Broadband PCS	Ended: 2/15/2005	\$2.0 billion

(*) Very little actually collected due to bankruptcy of winning bidder Nextwave

(**) About \$4 billion uncollected due to Nextwave bankruptcy

SOURCE: Federal Communications Commission

In this story:

**BEACHFRONT BONANZA
NO HOLE POKING**

Sidebars:

**Frontline exposure for
startup firm**

NO HOLE POKING

Google and the two satellite-TV providers have endorsed combinatorial bidding, which allows a bidder to win a package of individual licenses without needing to place the highest bid on each one up for auction, according to game theory.

Such a bidding system is intended to facilitate assembly of a national footprint made up of multiple licenses and to frustrate the ability of another bidder to poke holes in the package by acquiring licenses in just a few key markets. DirecTV and EchoStar favor national wireless coverage to complement the 50-state marketing of their video services.

Google, along with MAP and allies, have endorsed anonymous bidding. They claim that keeping the identity of bidders a secret during the auction would prevent cable and phone incumbents from blocking new entrants or artificially driving up their license-acquisition costs.

Google, the dominant Web-search engine, hasn't declared whether it will be a bidder. But it has taken an active interest in 700-MHz issues as part of an effort to ensure that broadband network owners don't shake down Web-based providers of content and services.

"Universal accessibility is one thing that is out of our control. We rely completely on the underlying infrastructure on both the wireline and wireless sides to actually carry our applications to our end users," said Google's Whitt.

In response, SpectrumCo filed comments with the FCC urging rejection of large spectrum blocks, saying the agency needed to vary the sizes to accommodate the needs of many different bidders. It also dismissed combinatorial bidding and anonymous bidding as untested concepts that would likely decrease the efficiency of the auction.

"Rather than trying to 'pick winners,' and either implicitly or explicitly giving certain entities a boost through eligibility restrictions and peculiar service rules ... the FCC should allow market forces to determine the winners of the 700-MHz auction," SpectrumCo attorney Michele Farquhar said in an FCC filing.

It wasn't until 1993 that the FCC obtained the legal authority from Congress to license spectrum via auctions or, as it is known in the law, "competitive bidding." Awarding licenses to the highest bidder was a radical change. In the early 1980s, for example, the FCC created two cellphone licenses for every market in the country. But it gave one of them to each local phone company for free and assigned the others by lottery, a transfer of wealth from taxpayers to private interests worth billions of dollars.

1981: FCC created two cellular phone licenses in each market, giving away one of them to each local telephone incumbent.

1983: FCC distributed second cell license by lottery.

1993: Congress gave FCC authority to conduct spectrum auctions for first time.

1994: In first auction, the FCC raised \$617 million for U.S. Treasury.

2006: Congress ordered FCC to auction in 2008 about 60 MHz of spectrum in 700 MHz band being vacated by local TV stations in February 2009.

2007: Total revenue after 68 FCC-conducted auctions over 13 years: \$28 billion.

SOURCE: *Multichannel News* research

Except for the FCC's multibillion-dollar mishandling of two auctions related to the bankruptcy of startup entity Nextwave Personal Communications, spectrum auctions have been a success. Over the course of 63 auctions, the agency has collected about \$28 billion for the U.S. Treasury.

Auctions also ignited the mobile communications market. In 1993, 16 million Americans were wireless subscribers, using handsets that resembled bricks. Today, 230 million people in the U.S. subscribe to a wireless provider, porting around sleek handheld devices that make calls, send e-mail, snap photos, and play video clips.

"The average bill, interestingly, in 1993 was \$61.50. It's declined now to \$50," said Entertainment Software Association president Michael Gallagher, who was Assistant Secretary of Commerce for Communications and Information until early 2006.

SpectrumCo's \$2.4 billion investment in the AWS spectrum last year gave it coverage of about 90% of the U.S. population. Comcast owns 52% of SpectrumCo while Time Warner Cable has 29% and Sprint just 5%.

Sitting on spectrum doesn't make economic sense, the industry maintains.

"The notion that cable operators would, in this already competitive environment, purchase spectrum in the 700-MHz auction for the purpose of 'warehousing' it in order to thwart additional competition in the provision of broadband services is absurd," the NCTA told the FCC. "Such warehousing would also not be welcome by the financial markets, which, of course, do not reward wasteful spending."

FCC officials haven't indicated whether they want to exclude cable and phone companies or whether 700 MHz license winners would need to divest a proportional amount of AWS spectrum.

"The key issue for investors is whether there will be new wireless/broadband entrants or whether this will be another incumbent sweep," Stifel Nicolas wireless market analyst Rebecca Arbogast said in a recent client note, referring to the large number of AWS licenses captured by cable companies, T-Mobile, AT&T and Verizon. Final FCC rules should emerge no later than early August, she said.

Last year, Congress passed a law ordering the FCC to auction 60 MHz in the 700-MHz band. The \$10 billion expected from the auction — which must begin not later than Jan. 28, 2008 — is needed to underwrite a \$1.5 billion consumer-coupon program for digital-to-analog TV converter boxes and \$1 billion for public-safety communications equipment.

Years ago, the FCC set aside 24 MHz in the 700-MHz band for use by the nation's 40,000 public safety groups, which will get their chance to use it when the TV stations clear out in about 20 months. About half the public safety spectrum is designated for broadband services.

As FCC leaders deliberate, lobbying has been heavy on what regulations should apply to the mobile services offered by winning 700-MHz bidders.

The public-interest groups, for example, have insisted that 700-MHz winners comply with network neutrality rules and lease 50% of their capacity to third parties on non-discriminatory terms and conditions.

Public Knowledge president Gigi Sohn said European countries have embraced the open-access model she wants imposed on 700-MHz winners.

“That’s why you see far greater speeds there, far better prices,” she said.

Frontline exposure for startup firm

Adding to the battle is a startup that is advocating combining public-safety and commercial spectrum in the 700-Mhz band, as an alternative to the purely commercial interests of cable and telephone companies. Leading its effort: two former Federal Communications Commission chairmen.

The company, Frontline Wireless, has promised to build for free a broadband network that will serve every fee-paying public-safety organization in the country. Such a network — which could cost \$15 billion to build — would be designed to achieve the long-sought goal of ensuring that first responders from multiple jurisdictions can routinely communicate while confronting the same crisis.

Making the pitch: Reed Hundt, FCC chairman from 1993 to 1997, who is Frontline’s vice chairman. Mark Fowler, FCC chairman under President Reagan, is a founding partner and investor in Frontline.

“It would be a dream come true for public safety in America to have the private sector build them for free a national wireless broadband network,” said Hundt, who as FCC chairman in 1994 crafted the first spectrum auction.

Other Frontline promises include: leasing all of its spectrum on a wholesale basis, with 25% of capacity allocated through a real-time auction proposed by Google.

Backed in part by Google directors John Doerr and Ram Shriram, Frontline has run into some resistance. Although Frontline intends to acquire 10 MHz of spectrum — the so-called E Block — in the auction, it wants the FCC to bless its use of 12 MHz of public safety spectrum to provide commercial service during normal times.

This even though, in 1998, the FCC designated 24 Mhz of the 700-Mhz band for public-safety purposes.

As a result, not all potential auction participants believe public safety organizations need any more spectrum in the 700-Mhz band.

“Public-safety [organizations] have 24 Mhz of spectrum that they haven’t been able to come together and agree on” how to use, said Gil Perez, CEO of Arcadian Networks, a Valhalla, N.Y.-based startup with \$90 million of backing, largely from Goldman Sachs. “Why do you need a new green patch? Why don’t they mandate utilizing the existing patch?”

Arcadian bought 2- and 4-MHz slices of the spectrum in April 2005, believing the frequencies were underutilized.

The company bought its chunks on secondary markets, from the FCC; and now has spectrum worth an estimated \$368 million, in 23 states.

It is focusing on getting what it calls “anchor” customers in its networks: energy and utility companies. Arcadian offers to upgrade their towers and existing networks; and, if successful, then will resell bandwidth to “tenants” such as manufacturers, mining companies and other companies with widely dispersed operations in rural parts of the country.

This includes border patrol agencies and other public safety institutions. “There is an ability to solve this problem, with market forces,” says Perez. “There’s no need to give billions of dollars to somebody. If you go with the Frontline proposal, you will reduce the value of the spectrum.”

SpectrumCo suggested that Frontline’s rule-heavy plan appeared to be designed to ensure that only Frontline won the E Block auction, depressing revenue. New York City — symbolically important because the Sept. 11, 2001 terrorist attacks destroyed the World Trade Center in lower Manhattan — stressed that because the FCC likely didn’t have authority to allow commercial use of the public safety spectrum, the agency was inviting litigation. A court case could delay the start of the auction and postpone receipt of the \$2.5 billion earmarked for first responder equipment and DTV converter boxes.

— *Ted Hearn and Tom Steinert-Threlkeld*

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