

February 16, 2005

**To:** National ITFS Association Conference Attendees

**From:** Robert J. Rini

### **EBS Leases – Comparison of Existing Lease Requirements to “New” Secondary Market Lease Requirements**

This memorandum summarizes the new set of rules and policies that, as of January 10, 2005, now govern the Educational Broadband Service (“EBS”) and Broadband Radio Service (“BRS”).

Under the new rules, licensees may enter into three different types of spectrum lease agreements:

- spectrum manager leases
- long-term *de facto* transfer leases
- short-term *de facto* transfer leases

Generally speaking, the spectrum manager lease form is more like the airtime lease form most are familiar with, whereas the *de facto* transfer lease form offers a new option to licensees that desire to be less involved in day-to-day matters and to reduce accountability to the FCC. With this understanding, as explained in more detail below, you can better appreciate how the relationship between EBS licensees and their spectrum lessees may need to be altered, and can better evaluate the risks and opportunities that will exist.

#### ***Summary***

There are a number of changes to the leasing rules and policies. Following are three major points that should be considered when negotiating and drafting EBS capacity leases:

- Lessees now have the ability to negotiate for greater control over the leased spectrum, although the EBS licensee must retain *ultimate* responsibility for complying with FCC rules regarding station construction and operation.

- Leases now need to contain specific language describing the rights and obligations of the parties with respect to each other and the FCC, including provisions addressing termination of the license, assignment of the lease and possible FCC enforcement action against a lessee.
- Licensees and lessees now need to either notify the FCC (for a spectrum manager lease) or obtain prior FCC approval (for a *de facto* transfer lease or if certain exceptions for spectrum manager leases apply to EBS or BRS) before operations under the lease may begin, but will not be required to submit copies of the lease.

### ***Background***

On October 6, 2003, the FCC released new rules for certain Wireless Radio Services that would permit, in many cases for the first time, leasing of spectrum capacity.<sup>1</sup> The Commission authorized three kinds of secondary market leases – spectrum manager leases, long-term *de facto* transfer leases and short-term *de facto* transfer leases – and adopted rules and policies applicable to each. Depending on the type of lease, some form of FCC notification or approval will be required before operations under the lease may begin, and the Commission has established rules that generally allocate compliance obligations proportionate to the level of control delegated to the lessee.

In a further notice of proposed rulemaking included in the *Secondary Markets Order*, the Commission, among other things, requested comments on whether and to what extent the secondary markets rules should extend to BRS and EBS. Subsequently, all of the comments addressing this issue were considered in the rebanding proceeding. In the Report and Order released July 29, 2004, the Commission extended the secondary market leasing policies to BRS and EBS.<sup>2</sup> The Commission stated that leases entered into before the effective date of the new rules would be grandfathered, and “leases entered into pursuant to the former Part 74 rules may be renewed and assigned in accordance with the terms of such lease.”<sup>3</sup>

The Commission also determined, however, that its existing “substantive use requirements” for EBS would continue to apply. These are believed to include some or all of the following:

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<sup>1</sup> See *In the Matter of Promoting Efficient Use of Spectrum Through Elimination of Barriers to the Development of Secondary Markets*, Report and Order and Further Notice of Proposed Rulemaking, WT Docket No. 00-230, FCC 03-113 (rel. October 6, 2003) (“*Secondary Markets Order*”).

<sup>2</sup> See *Amendment of Parts 1, 21, 73, 74 and 101 of the Commission’s Rules to Facilitate the Provision of Fixed and Mobile Broadband Access, Educational and Other Advanced Services in the 2150-2162 and 2500-2690 MHz Bands*, Report and Order and Further Notice of Proposed Rulemaking, 19 FCC Rcd 14165 (2004) (“*Rebanding Order*”).

<sup>3</sup> Section 27.1214(d) of the Commission’s Rules.

- There must be minimum educational use of the spectrum (20 hours per 6 MHz channel per week).
- The licensee must have the right to recapture additional capacity for educational purposes (5% for digital).
- Lease terms can not exceed 15 years.
- The licensee must remain ultimately responsible for complying with FCC rules regarding station construction and operation.
- Only the licensee can file for license modifications.
- The licensee must have the right to access transmission equipment (or comparable equipment) upon termination of the lease as a result of the lessee's actions.<sup>4</sup>

Many of these requirements are set forth in new Section 27.1214 of the Commission's Rules, and are now effective. The rules, however, do not incorporate the maximum lease term and the licensee's obligation to comply with construction and operational rules. The Catholic Television Network and the National ITFS Association have asked the FCC for clarification of these points. They also have requested the FCC to clarify rules regarding the rights of EBS licensees to acquire equipment at the end of the lease.

On September 2, 2004, the Commission released a Second Report and Order in the secondary markets proceeding.<sup>5</sup> Among other things, the Commission streamlined its lease approval process and extended its leasing policies to additional wireless services. The Commission also authorized "private commons" arrangements, in which a licensee or spectrum lessee makes certain spectrum usage rights available to third-party users employing advanced communications techniques that involve peer-to-peer (device-to-device) communications and that do not use an end-to-end physical network infrastructure.

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<sup>4</sup> *Rebanding Order*, ¶181.

<sup>5</sup> See *In the Matter of Promoting Efficient Use of Spectrum Through Elimination of Barriers to the Development of Secondary Markets*, Second Report and Order, Order on Reconsideration, and Second Further Notice of Proposed Rulemaking, should be a better FCC Rcd cite. These rules will be effective February 25, 2005.

## *EBS Leases*

Historically,<sup>6</sup> EBS leases have been subject to the *Intermountain Microwave* guidelines for determining whether the licensee retains *de facto* and *de jure* “control” of its facilities.<sup>7</sup> The *Intermountain Microwave* standard looks to six criteria to determine whether a licensee has abdicated control in favor of another party:

- unfettered use of the facilities
- control over day-to-day operations
- policy decisions
- personnel decisions
- responsibility for financial obligations
- receipt of moneys<sup>8</sup>

The Commission considers these criteria by reviewing the “totality of the circumstances,” which includes examining not just the agreement between the parties, but the actions of the parties.

Over the years, several lease templates have evolved that incorporate the *Intermountain Microwave* guidelines and the “substantive use requirements” that apply uniquely to EBS in view of its educational purpose. The following discussion compares and contrasts the traditional leasing model with the EBS models that are developing under the secondary market rules.

## *Comparative Analysis*

*FCC Compliance and Licensee Control.* Under a spectrum manager lease, the licensee remains primarily and directly responsible for ensuring compliance with FCC rules and policies. The licensee must take all reasonable steps necessary to ensure compliance by its lessee, and is subject to FCC enforcement action if a lessee violates FCC rules and policies. The licensee must retain operational oversight over the leased spectrum and must have the right to inspect the facilities. The lessee must cooperate fully with any investigation or inquiry and must allow the FCC or the licensee to conduct on-site investigations or suspend operations in certain cases.

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<sup>6</sup> The FCC first authorized leasing of EBS excess capacity in 1983 when it re-allocated the E-Group and F-Group channels to BRS. See *Amendment of Parts 2, 21, 74 and 94 of the Commission’s Rules and Regulations in Regard to Frequency Allocation to the Instructional Television Fixed Service, the Multipoint Distribution Service, and the Private Operational Fixed Microwave Service*, Gen. Docket No. 80-112 and CC Docket No. 80-116, Report and Order, 94 FCC 2d 1203 (1983).

<sup>7</sup> See *Intermountain Microwave*, 12 FCC Rcd 559 (1963).

<sup>8</sup> See also, e.g., *Millicom of Omaha, Inc.*, 63 RR2d 1011, 1015-16 (1987) (regarding a “turnkey” cellular management agreement).

Under a *de facto* transfer lease, the lessee is primarily and directly responsible for such compliance, and is independently accountable for compliance. The lessee is in all respects subject to Commission enforcement, though the licensee may be liable for ongoing violations or egregious behavior by the lessee about which the licensee knew or should have known. A *de facto* transfer lease will afford lessees greater ability to exercise control over the licensee's spectrum and, accordingly, the lessee assumes greater responsibility to comply with FCC rules and subjects itself to direct FCC enforcement.

Reading the *Secondary Markets Order* and the *Rebanding Order* together, and as confirmed by informal FCC advice, for either a spectrum manager lease or a *de facto* transfer lease, the "substantive use requirements" for EBS continue to require the EBS licensee to retain *ultimate* responsibility for complying with FCC rules regarding station construction and operation, consistent with the requirements for existing ITFS leases. According to FCC staff, there is a distinction between *ultimate responsibility*, which must reside with the EBS licensee, and *primary and direct responsibility*, which may be delegated to a lessee under the *de facto* transfer lease model. FCC staff also confirmed that it did not intend to restrict EBS *de facto* transfer leases. As discussed above, CTN/NIA have asked the Commission to clarify that EBS licensees can enter into *de facto* transfer leases and that certain "substantive use requirements" therefore would not apply.

In some cases, EBS licensees may insist on retaining control consistent with a spectrum manager relationship, while in other cases, the lessee may desire to be more active in overseeing FCC matters. Regardless of what lease option is negotiated, the lease should clearly recite the allocation of responsibilities, particularly as they relate to direct and primary responsibility for complying with FCC rules and policies.

*FCC Approval of Leasing Relationship.* Rules in the former ITFS service generally required ITFS applicants and licensees to submit copies of their excess capacity leases to the FCC. The Commission retains oversight of leases to ensure that the lease complies with the substantive use requirements. In some cases, FCC staff has required licensees to amend an ITFS lease to provide missing language, such as recapture or equipment purchase, and has not granted an ITFS application until the lease is brought into compliance. In other cases, the FCC has taken no action on leases. At best, the FCC's historical enforcement of its policy requiring submission of ITFS leases for its approval has been spotty and inconsistent.

In the rebanding proceeding, the Commission requested comment on whether it should continue its practice of requiring submission of leases. The Commission did not address this issue directly in the *Rebanding Order*, apparently concluding that the general applicability of the secondary markets rules would apply. FCC staff has informally advised us that EBS leases will not need to be submitted to the Commission. However,

both the licensee and the lessee must retain copies of the lease, and the Commission has the right to ask for copies.

Under rules announced in the Second Report and Order in the secondary markets proceeding, the FCC will immediately and automatically approve commencement and extension of the leasing relationship, and assignment of the lease, on the business day immediately following the filing of the lease notification (for spectrum manager leases) or application (for *de facto* transfer leases) on new FCC Form 603-T. Immediate approval will not be available when there are issues concerning the lessee's eligibility, basic qualifications or foreign ownership. Also, immediate approval is not available for a lease involving spectrum that is, or may reasonably be, used for "interconnected mobile voice and/or data services" where there would be a geographic overlap with other spectrum used to provide services in which the lessee holds a 10% or more interest as a licensee or lessee. The Commission will rely on the certifications of the lessee with respect to eligibility issues. Petitions for reconsideration can be filed within 30 days following public notice of the approval of the leasing relationship.

Most likely, immediate approval will not be available for EBS leases or material amendments to existing leases entered into under the new rules. The Commission specifically named BRS as a service subject to competitive inquiry, and it is believed that EBS assignments, transfers and leases would not be considered for "overnight" approval. Moreover, a lessee must certify that meets the basic qualifications for holding the license associated with the lease and that it will comply with all applicable use restrictions.

If the immediate processing rules do not apply, notification of spectrum manager leases must be filed at least 21 days before commencing operations (10 days if the spectrum manager lease is for less than a year) or extending the leasing relationship beyond the initial term. Applications for long-term *de facto* transfer leases (which must be accompanied by a filing fee) will be placed on public notice and the Commission will act on the application within 21 days. If the FCC determines that the application is subject to further review, it must complete the review within 90 days. The FCC will issue a separate authorization to the lessee under a *de facto* transfer lease.

*Lease Term.* Policies historically prescribed a 15-year maximum term for leases, subject to renewal of the license. Subject to resolution of the request of CTN/NIA to affirm that EBS lease terms will continue to be limited to 15 year terms, the term limits for spectrum manager and *de facto* transfer leases are the same, and specifically permit leasing activity to continue while a notification or application for extension of the leasing relationship is pending before the FCC as part of the license renewal process.

*Termination of Lease.* A lessor (also the licensee) under a spectrum manager lease must have the right to terminate the lease if the lessee does not comply with the terms of the lease and FCC rules and policies. If a lessee violates FCC rules or causes

harmful interference, the licensee must have the right to remedy the violation or interference. Under a *de facto* transfer lease, the licensee's oversight is reduced, but it may still be liable for ongoing violations or egregious lessee behavior. The lease may contain provisions that ensure that the licensee will not "arbitrarily terminate" the lease.

*Interference.* For a spectrum manager lease, the licensee is responsible for coordinating operations and resolving interference-related matters, including those between its lessee and third parties. The licensee also is responsible for determining whether modification applications will be required and complying with environmental and safety rules. For a *de facto* transfer lease, primary responsibility for these actions shifts to the lessee.

*Interactions with FCC.* As is the case with existing ITFS leases, the licensee under a spectrum manager lease remains responsible for interacting with the FCC and making all FCC filings. Under a *de facto* transfer lease, the lessee can assume these responsibilities.

### ***Conclusion***

The secondary markets rules afford additional flexibility to permit a lessee to exercise more control over the spectrum and the facilities pursuant to a *de facto* transfer lease. Regardless of the category of lease, many of the historical "substantive use requirements" for EBS will continue to apply. Whether parties enter into one kind of lease or another should depend on the educational objectives of the licensee and the economic impact and degree of control that the parties desire.

Please contact us if you have any questions.