June 3, 2003

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Policy Branch
International Bureau

The Honorable Michael K. Powell
Chairman
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: TMI Letter of Intent Authorization and Assignment to TerreStar
File No. 189-SAT-LOI-97; IBFS Nos. SAT-LOI-19970926-00161, SAT-AMD-20001103-00158, SAT-MOD-20021114-00237, SAT-ASG-20021211-00238

Dear Chairman Powell:

Ex parte meetings with the International Bureau over the past few weeks about the above matter have identified three issues on which the staff expressed an interest in further information and comment, and which may interest the full Commission before whom the matter is pending: (1) the experience in other communications services regulated by the FCC where third parties have assumed responsibility for performing obligations under the FCC license; (2) whether TMI, as the authorization holder here, retained control over the construction necessary to meet the milestone requirement; and (3) an analysis of the contractual relationships and obligations between and among TMI, TerreStar, and Loral. In fact, the three lines of inquiry merge.

Experience in Other FCC-Regulated Services

TMI and TerreStar were asked about their assertion that, in other FCC-regulated services, licensees frequently arrange for third parties to perform their obligations, specifically construction obligations, under the applicable FCC authorizations. Supporting this assertion, TMI/TerreStar's Application for Review and Reply referred in the broadcast services to local marketing agreements and purchase arrangements where the time broker or buyer undertakes certain licensee responsibilities, and in the wireless services to arrangements where investors, would-be purchasers, or neighboring system operators construct or operate the systems or both.

In the context of broadcasting local marketing agreements, the Commission only requires that licensees retain "ultimate control"; they may delegate all "day-to-day operations . . . as long as [the licensees] continue to set the policies guiding those operations." *Radio Moultrie*, FCC 02-319 (Nov. 26, 2002). In the cellular and PCS services, McCaw Cellular and other third parties built out scores and perhaps hundreds of construction permits for FCC licensees. Such arrangements were particularly prevalent for wireless licenses awarded in

auctions in which designated entities participated. For example, in Auction No. 35, the FCC required PCS licensees (on Exhibit E to the long form) to disclose a variety of agreements. A number of license applications by designated entities described technical service agreements in which a major wireless carrier agreed to provide all operational, engineering, maintenance, construction, insurance, repair and other technical operations of the facility, subject to the licensee's ultimate control. These applications were subsequently approved by the Commission in the ordinary course because such third party operations are entirely consistent with a licensee retaining control of the license.

Because such arrangements were and are so routine in these other services, and do not require express Commission approval (though the Commission has consistently approved transfer and license applications which describe such arrangements), these kind of arrangements have not been litigated and so we are not aware of any cases that specifically uphold them against challenge or scrutiny. But that is not surprising given that with these other services, the Commission's concern is not about whether a third party performed the work necessary to meet obligations under the license, but instead about whether the licensee has retained sufficient control over the activities of the third party necessary to keep the license in good standing. The leading case on control in these circumstances is *Intermountain Microwave*, 12 F.C.C.2d 559 (1963). Before turning to the case law on this issue, a perhaps obvious point bears mention: the Commission's concern about control necessarily assumes the propriety of third-party arrangements, if properly carried out. The Commission's insistence on the licensee's retaining control inarguably means that such arrangements are appropriate, even desirable, and that the issue, instead, is a matter of how the arrangements are structured and performed, not whether they are permissible.

The FCC's Jurisprudence on Control

In *Intermountain*, the Commission adopted a multifactored, fact-specific test for licensee control. "The normal minimum incidents" of licensee control, the Commission held, "include the unfettered use of all facilities and equipment used in connection therewith; day to day operation and control; determination of and the carrying out of policy decisions, including the preparation and filing of applications with this Commission; employment, supervision, and dismissal of personnel; payment of financial obligations including expenses arising out of operation; and the receipt of moneys and profits derived from the operation of the . . . facilities." *Intermountain*, 12 F.C.C.2d at 560. Importantly, the Commission distinguished between the ownership and control of the license, and the ownership and control of the operating facilities: "Ownership of the [operating] facilities by someone other than the licensee is not necessarily inconsistent with these incidents of control." *Id.* Under the Commission's traditional analysis of control, arranging for another party to construct or operate the facility also is "not necessarily inconsistent with these incidents of control."[1]

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[1] The Commission's shift away from *Intermountain* last month is of course not relevant to the present case as a procedural matter because it occurred after the fact; and substantively, the recent decision does not change the calculus because if the applicant meets the *Intermountain* test it certainly meets the new test under this "new world (continued...)

Contractual Analysis

The focus on control funnels the analysis to the contractual relationships involved here – a fact-specific analysis of the kind required under *Intermountain*.

TMI has control: That analysis must start with the TMI/TerreStar contract of July 12, 2002, which was submitted to the Commission on July 26, 2002. The first "Whereas" clause of that contract recites that TMI holds the Canadian license and U.S. authorization. The second "Whereas" clause explains that TMI intends to transfer the Canadian licensee to an entity, eligible under Canadian law, in which TerreStar or TMI will have an interest. The third "Whereas" clause states a parallel intention to transfer the U.S. authorization to a "suitable entity" in which TerreStar or TMI will have an interest. The next "Whereas" clause recites the parties' intention to commence "satellite construction in a timely manner and thereby satisfy certain [Canadian and U.S.] milestone requirements." And the last "Whereas" clause states that "*TMI has exercised oversight and direction in the development of a proposed satellite procurement contract*" with Loral, which has fully engaged in constructing the satellite (emphasis added). This last clause, of course, attests to TMI's control over the required satellite construction process, and the record contains nothing that rebuts that evidence. Nor could it be rebutted, for in fact TMI has retained control.

The next paragraphs of the contract sets forth, first, the obligations TMI imposed on TerreStar and, then, the obligations which in turn TMI is bound to TerreStar to perform. In the first of these, TMI obligates TerreStar, "within the [Canadian and U.S.] milestones," to enter into "a *non-contingent* satellite procurement contract with Loral" (emphasis added). Under the terms of the provision, that procurement contract must be "satisfactory to TMI" and must be consistent with the Canadian and U.S. authorizations. The provision goes further: "TMI shall retain control over the content and delivery of the satellite," so long as it holds the Canadian and U.S. authorizations. It is hard to imagine contractual language that would more effectively assure TMI control. These provisions should put the issue of control to rest.

TMI is obligated: TMI and TerreStar do not agree with the International Bureau that TMI must be directly "obligated" to Loral; it should be enough that Loral is obligated to construct and that construction is proceeding as required, both of which are the case here. But our differences with the International Bureau on this legal point are irrelevant *because TMI has commensurate obligations to perform.*

TMI's being obligated is made clear by the next provisions in the TMI/TerreStar agreement. Those provisions recite that TerreStar is providing consideration to TMI by contracting for construction of the satellite by Loral. In exchange for this consideration, TMI is obligated, "at TerreStar's election," to "expeditiously transfer" the Canadian and U.S.

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of spectrum flexibility." Joint Statement of Chairman Powell and Commissioner Martin, WT Docket No. 00-230 (May 15, 2003).

authorizations "to the entities noted above . . . subject to any necessary Canadian or United States regulatory approvals." The next provision of the agreement provides that at that point, TMI shall "transfer all of its right, title and interest in and under the Loral contract."

Inherent in TMI's obligation to TerreStar to transfer the authorization is an obligation to maintain the Canadian and U.S. authorizations in good standing until such time as the authorizations are transferred to the entity designated by TerreStar. As the seller of valuable assets, TMI must preserve the assets that it has agreed to transfer to TerreStar, and it cannot undercut, compromise, jeopardize or, in the words of Bureau staff, "walk away from" the Canadian and U.S. authorizations. If TMI attempted to walk away – and it clearly has not attempted to do so – TerreStar would have the right under the agreement to require TMI to take whatever steps are necessary to preserve the authorizations until such time as the authorizations were transferred to TerreStar. As a matter of contract law, that is crystal clear.

The FCC May Rely on Private-Party Contracts. The Commission can and should rely, and has relied, on this reasoning. It is the reasoning that underlies the Commission's day-in, day-out willingness to allow third party contracts – entered into by time brokers and buyers in the broadcast services and adjacent cellular operators and investors in the wireless services – to satisfy licensee construction and operating obligations. TMI is a well-established, experienced Canadian company which has no intent of jeopardizing the Canadian and U.S. authorizations, but, even apart from its reputation, its agreement with TerreStar would preclude its walking away from the authorizations.

The Bureau's Order (¶ 10) acknowledges that it has permitted third parties to discharge satellite construction obligations but states that it has done so only in parent/subsidiary situations. However, it is the contractual obligation between the parties, not an ownership relationship, that should be determinative. With a contract, Company A is bound to preserve the FCC authorization that it has agreed to sell to Company B. In contrast, without a contract, a subsidiary would not have a legal obligation to maintain an FCC authorization for the benefit of a parent or vice versa. It is well settled under corporate law that a corporate parent can take a course of action that is inconsistent with or adverse to the interests of a wholly owned subsidiary; the parent does not even have to act fairly – it has no fiduciary duty to the subsidiary in that situation. *See* 1-15 Delaware Corporation Law and Practice § 15.11 (2002). Thus, the parent/subsidiary relationship, which seems so important to the Bureau's analysis, in fact is a less reliable basis for finding an obligation than is a contractual relationship such as existed here between TMI and TerreStar.

The Canadian decision should be given weight: Industry Canada's August 23, 2002, letter finding that TMI was "obligated" (and that the Canadian milestone was met) is significant, in part, because that conclusion was based on the contractual obligations between TerreStar and TMI. It is not a conclusion based on interpreting Canadian regulatory law but on interpreting a contract, and Canadian and U.S. contract law is similar. In retrospect, TMI and TerreStar perhaps should have explained in greater detail the business plans, including satellite design and procurement and the relationships of the parties, with the FCC's International Bureau, and they regret that this failure has resulted in misunderstandings about TMI's rights and obligations.

Summary: In short, TerreStar was and is obligated to TMI to enter into and perform an appropriate construction contract with Loral, and TMI is obligated to TerreStar to take the appropriate steps to preserve the authorizations until they are transferred to TerreStar. These obligations arise under agreements that enable the affected parties to take appropriate legal action to enforce the rights created by the contracts. As a consequence, these agreements are binding and enforceable and thus satisfy the Commission's requirement that a party be "obligated."

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Based on the following factors, TMI and TerreStar continue to believe that the FCC's milestone requirement was met.

- The requisite construction was performed, was paid for ($800,000), and is continuing.

- The FCC and especially the courts have held that the more draconian the punishment (here it is the death penalty), the more explicit the Commission requirement must be that was allegedly violated.

- In no case, not even in the satellite service, has the FCC ever cancelled an authorization where the required construction has been performed on the basis that the licensee was not the direct contracting party or directly obligated to the entity constructing the satellite.

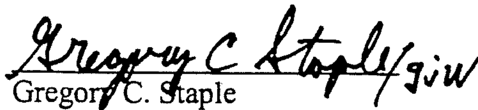
- WTO considerations argue that respect be paid to Industry Canada's licensing and milestone processes.

- No one would be hurt by a determination that the milestone was met and the public interest (more service, more competition) would be served.

At the last meeting with the International Bureau, we were asked about the appropriateness of a waiver in these circumstances. Notwithstanding our conviction that the milestone was met, we responded that the Bureau (or the full Commission) could conclude that, in the future, satellite licensees must be in a direct contractual relationship with the satellite construction contractor, but for reasons relating to the above factors, the Bureau (or Commission) could waive that requirement here. Through a waiver, the Commission would preserve and confirm that it believes a direct contractual relationship is necessary between the licensee and satellite contractor, but it would also achieve a just result here that serves the public

interest in these particular circumstances. The D.C. Circuit Court of Appeals has held that the FCC must take a "hard look" at waiver requests, finding that limited waivers of general rules are "the very stuff of the rule of law." *WAIT Radio v. FCC*, 418 F.2d 1153, 1158-1159 (D.C. Cir. 1969).

Respectfully submitted,



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