Broadcasting Licenses: Ownership Rights and the Spectrum Rationalization Challenge

Why the Government is Buying Back its Own Spectrum

[Presented at Columbia Law School - November 8, 2012]
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Who Am I?

- J. Armand Musey, CFA
President/Founder, Summit Ridge Group, LLC

Industry Background

- Blend of 16 years of equity research, investment banking and consulting experience including
  - Top Ranked Equity Research Analyst
    - Three-time Institutional Investor “All American” Ranking
    - #1 Ranked by Greenwich Association poll of institutional investors
    - Wall Street Journal “Best on the Street” ranking
  - President of small boutique investment bank
  - Extensive Consulting Experience

Education/Training

- JD/MBA (Northwestern); MA (Columbia); BA (U. Chicago)
- Chartered Financial Analyst (CFA)

Other

What do I do
What am I going to talk about?
- Two Papers

• Broadcasting Licenses: Ownership Rights and the Spectrum Rationalization Challenge

• How the Traditional Property Rights Model Informs the Spectrum Rationalization Challenge
Outline of Presentation

- Background on FCC Spectrum Reallocation
- No Legal Basis for Property Rights to Spectrum
- But Significant Due Process Rights
- Leads to Meaningful Negotiating Leverage
  - Why is the government paying to reacquire its own assets?
  - How did this happen?
  - What is the best way out?
- Conclusion
  - What does this mean?
  - How did this happen?
  - How do we avoid this next time?
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Background – Demand for Mobile Wireless Data Growing Fast!

Source: FCC; National Broadband Plan
FCC Licenses Allocated for Specific Use

• Licensee can’t use for alternative purpose (much like zoning)

• Spectrum shortage for broadband, but inefficient use for other applications (need new zoning plan) – most of TV broadcasting spectrum nationwide is unused

• According to the FCC Chairman, if our nation does not address spectrum availability issues we will face:
  • “higher prices, poor service quality, an inability for the U.S. to compete internationally, depressed demand and, ultimately a drag on innovation”
Currently 547 Mhz for Mobile Broadband

Source: FCC; National Broadband Plan, Exhibit 5-F: Spectrum Baseline
# FCC Wants to Add 300 Mhz More

<table>
<thead>
<tr>
<th>Band</th>
<th>Key Actions and Timing</th>
<th>Megahertz Available for Mobile B-band</th>
</tr>
</thead>
<tbody>
<tr>
<td>WCS</td>
<td>2010—Order</td>
<td>20</td>
</tr>
<tr>
<td>AWS 2/3</td>
<td>2010—Order; 2011—Auction</td>
<td>60</td>
</tr>
<tr>
<td>D Block</td>
<td>2010—Order; 2011—Auction</td>
<td>10</td>
</tr>
<tr>
<td>Mobile Satellite Services (MSS)</td>
<td>2010—L-Band &amp; Big LEO Orders; 2011—S-Band Order</td>
<td>90</td>
</tr>
<tr>
<td>Broadcast TV</td>
<td>2011—Order; 2012/13—Auction; 2015—Band trans/clearing</td>
<td>120</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>300</strong></td>
</tr>
</tbody>
</table>

*Source: FCC; National Broadband Plan*
Background - Current Situation

- FCC seeks to reallocate significant amounts of TV spectrum for mobile broadband use
  - Undeniably underutilized as approximately 90% of households watch television on cable/satellite
  - Economically inefficient
    - Television spectrum license trade for about $0.10 - $0.15 per Mhz/POP
    - Mobile broadband spectrum trades at over $1.00 per Mhz/POP
      - demand is soaring!
    - A small fraction of the difference could subsidize basic cable for the 10% of over the air viewers
  - Economists point to a multiplier effect in terms of cost to society
  - Public policy analysts point to additional social benefit
Initial Questions

• 1) Do the broadcasters have any legal property rights in their spectrum licenses?
• 2) If not, do they have any other rights?
• 3) What are other elements their bargaining position
Background - Electromagnetic Spectrum

- Owned by the Government
  - FCC created by the Communications Act of 1934 to manage spectrum use
  - FCC licenses spectrum to entities to use for limited duration “for the public good”
  - Licenses explicitly require licensees to waive ownership claims to the spectrum
  - Broadcasters received right to use the spectrum at no charge from the FCC
Background - Problem

• Government is in a position that it has effectively agreed to “buy out” the television broadcasters
  – Despite lack of any property rights
  – Despite FCC’s undisputed right to reacquire the licenses at the end of the license period
  – Moreover, government is committed to a “voluntary” auction process
• Essentially gives FCC license holders greater rights of control than private property owners have against government takeover
Background

• How did this Happen?????
Prior Related Academic Work Limited

Semi-Directly Related

Analogous Situations
3) Grazing Permit Litigation History

Other Applicable Law
1) Property Law Principles
2) Administrative Law Principles
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No Legal Basis for Property Rights

Text of Statutes and Legislation Preclude FCC Licensees from having property rights

- Communications Act of 1934 explicitly forbids any private property interest in electromagnetic spectrum
- 1996 Amendment to ‘34 Act confirms lack of licensee property rights
- FCC license themselves require license holders to disclaim any ownership interest
- No favorable legislative history for Broadcasters
No Legal Basis for Property Rights

- 1996 Amendment seems to almost guarantee renewal and forbid comparative evaluation process if broadcaster was acting “in the public interest.”
  - Comparative evaluation was based on current use not alternative use
    » May need a two step process to 1) determine the current use is not in the public interest and then 2) reallocate the spectrum
  - Legislative history suggests it was designed to curb abuse from preference bidders in renewal process
    » Not designed to limit the FCC from changing use to reflect technology changes
No Legal Basis for Property Rights

- Judicial precedent also precludes property rights
  - In analogous series of cases involving federal cattle grazing permits
    - Courts have repeatedly ruled they are not property (*U.S. v. Fuller* [SCOTUS, 1973], *Public Land Council v. Babbitt* [SCOTUS, 2000])
    - Courts have repeatedly rules licenses should be subject to strict textual interpretation (*Babbitt*)
    - In the few cases where courts have gone beyond textual interpretation, they’ve held that since the government exercised some control over licenses, it maintained ownership (*Fed. Land Legal Consortium v. U.S.* [10th Cir, 1999])
      - Would likewise apply to broadcasters as FCC has exercised even more control over them
No Legal Basis for Property Rights

- History of Renewals does not enshrine any property rights – but creates grounds for argument
  - FCC has renewed broadcasters’ licenses almost as a formality for decades
  - Statements from officials in all branches of government suggest renewals are to be expected
  - Renewal process has gotten easier over time
  - Possible Estopple argument is best hope for property rights
No Legal Basis for Property Rights

• Alternative Arguments fail
  – Promissory Estoppel
    • Licensees invested in businesses based on spectrum as FCC stood by esp. with digital conversion
    • Most investments were small and licensees are sophisticated players
    • Very hard to invoke promissory estoppel against the government (Office of Personnel Mgmt v. Richmond [SCOTUS, 1990])
    • Does not meet “unmistakability” test.
  – Adverse Possession
    • No evidence any of the FCC licensees are using the spectrum in an adverse manner
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But Significant Due Process Rights

• Congress could decide not to renew broadcaster’s licenses leaving broadcasters with limited recourse (Sidak and Spulber (Givings, Takings [1997]); also Verizon v. FCC [2002])
  – Not likely due to political pressure from broadcasters
    • NAB is powerful
    • Elected officials need support of their local broadcasters who can give them significant “news” coverage that eludes the equal time coverage requirements
But Significant Due Process Rights

• Absent new legislation broadcasters have significant due process rights
  – FCC would have to conduct a rulemaking process and possibly hold an adjudication for each license it chooses to not renew.
    • Each licensee with an unfavorable review would have the option of seeking judicial review
  – The cumulative administrative overhead of TV Broadcaster’s due process rights would be overwhelming
### Time-consuming Administrative Process

#### Time Historically Required To Reallocate Spectrum

<table>
<thead>
<tr>
<th>Band</th>
<th>First Step</th>
<th>Available for Use</th>
<th>~Lag Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Cellular (Advanced Mobile Phone System)</td>
<td>1970</td>
<td>1981</td>
<td>11 years</td>
</tr>
<tr>
<td>2) PCS</td>
<td>1989</td>
<td>1995</td>
<td>6 years</td>
</tr>
<tr>
<td>3) Educational Broadband Service EBS/Broadband Radio Service (BRS)</td>
<td>1996</td>
<td>2006</td>
<td>10 years</td>
</tr>
<tr>
<td>4) 700 MHz</td>
<td>1996</td>
<td>2009</td>
<td>13 years</td>
</tr>
<tr>
<td>5) AWS-1</td>
<td>2000</td>
<td>2006</td>
<td>6 years</td>
</tr>
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- Source: FCC: National Broadband Plan (Exhibit 5C).
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Why the Gov’t is Buying its Own Assets I

- Political Reasons – traditional argument
  - Broadcasters have significant political power
    - NAB is a powerful lobbying organization
  - Politicians want coverage from local broadcasters
    - News coverage of politicians is not subject to equal access regulation
  - Rural and Old Influence
    - Over the Air TV viewers are disproportionately rural and older
    - May lose some viewing choices
      » Have disproportionate political influence
Why the Gov’t is Buying its own Assets II

• Strategic Reasons – Does not want to upset settled expectations
  – If other licensees lose faith in their expected rights, they will likely bid less at auction for mobile broadband spectrum
    • Not paying the broadcasters may actually cost the government MORE!
    • They will be less likely to invest in deploying new advanced services

• To optimize motivation of other FCC licensees, it must treat broadcasters in a equitable manner

• Licenses have become integrated into larger framework
What is the Best Way Out?

• Consider an eminent domain framework
  – Government has essentially conceded the essential property right of control
  – Broadcasters reasonably treated licenses as property
  – Only need to pay current use value
    • A fraction of auction value for mobile broadband use
  – The framework is widely accepted and minimizes political debate
Gov’t Solution – H.R. 3630: Broadcasters get “Super” Property Rights

- A reverse auction to buy out broadcasters
- Resale at higher price
- Entirely voluntary
  - No ability to cancel licenses or “downgrade” during auction process
  - No process for dealing with holdouts
  - Possibility of upgrading spectrum if broadcaster broadcasts at least one channel
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View #1: Reality Outweighs Law

- Property Law
  - No Valid Legal Property Rights
- Practical Realities
  - Due Process Rights and Related Delays
  - Desire to Maximize Revenue from Future FCC Auctions
  - Political Power of Broadcasters
What Does this Mean?

- Private entities transformed temporary licenses of public property into something with the economic elements of their own private property
  - Essentially appropriated public assets with no legal basis
  - Private property was created extra-legally through network of dependencies and merely confirmed legally by legislation many year after the fact
View #2: (Future Work)
Old World Laws Fail in New Word

<table>
<thead>
<tr>
<th>Old World Model</th>
<th>New World Model</th>
</tr>
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<tbody>
<tr>
<td>“Pubic Trust” Model</td>
<td>“Private Property” Model</td>
</tr>
<tr>
<td>- Don’t pay for licenses</td>
<td>- Pay for licenses</td>
</tr>
<tr>
<td>- Less investment in business</td>
<td>- Major investment in buildout</td>
</tr>
<tr>
<td>- Fewer economic rights in licenses</td>
<td>- Expect greater economic rights</td>
</tr>
</tbody>
</table>

- FCC is operating in “New World” reality using “Old World” regulatory framework
  - It is forced into making clumsy adaptations

- Broadcasters got licenses in “Old Word” era and are returning them in “New World” era
  - Awkward for regulatory system to handle
How did this Happen?

• Government allowed, and encouraged an expectation based on a traditional technology – television broadcasting
  – Wanted to encourage investment in local programming despite the short-term (5 years, now 8 years) length of licenses
    • Gov’t officials from all sides were eager to give broadcasters assurances in the perpetual renewal of their licenses

• Other spectrum was licensed at fees that imply perpetual rights
  – FCC behavior is had downstream effects
  – Spectrum policy became part of a larger network of implications
Implications

• Government licenses in other areas may seek to turn temporary use licenses into ownership type rights
  – Grazing Permits
  – Mineral Licenses

• Government needs to shore-up regulatory framework to match current reality
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