DOCKET FILE COPY ORIGINAL

RECEIVED
APR 19 2001
FCC MAIL ROOM

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of:	)	
	)	
Amendment of Section 309(j) of the Communications Act -- Competitive Bidding for Commercial Broadcast and Instructional Television Fixed Service Licenses	)	MM Docket No. 97-234
	)	
Reexamination of the Policy Statement on Comparative Broadcast Hearings	)	GC Docket No. 92-52
	)	
Proposals to Reform the Commission's Comparative Hearing Process to Expedite the Resolution of Cases	)	GEN Docket No. 90-264

TO THE COMMISSION

PETITION FOR CLARIFICATION

David Honig
Executive Director
Minority Media and
Telecommunications Council
3636 16th Street N.W.
Suite BG-54
Washington, D.C. 20010
(202) 332-7005
mmtcbg54@aol.com

April 19, 2001

No. of Copies rec'd 0+11
List ABCDE

TABLE OF CONTENTS

	Page
SUMMARY	ii
BACKGROUND	1
I. THE BROADCAST AUCTION RULES CONTAIN A LOOPHOLE THAT COULD SIGNIFICANTLY DILUTE THE VALUE OF BIDDING CREDITS	3
II. THE COMMISSION SHOULD ENSURE THAT NO APPLICANT USES BIDDING CREDITS THE APPLICANT DOES NOT DESERVE	9
A. THE COMMISSION HAS NEVER BEFORE PERMITTED THE RETENTION OF COMPARATIVE BENEFITS BY APPLICANTS WHOSE STRUCTURES WERE NO LONGER CONGRUENT WITH THEIR COMPARATIVE BENEFITS	9
B. RECERTIFICATION OF OWNERSHIP STRUCTURES AT THE START OF THE AUCTION AND DURING EACH ROUND WOULD PREVENT MOST MISUSES OF BIDDING CREDITS	17
C. DISGORGEMENT, WITH A PENALTY FOR EARLY WITHDRAWAL OF A DIVERSIFICATION PROMISE, WOULD PROVIDE AN ADEQUATE REMEDY FOR COMPARATIVE DOWNGRADES AFTER THE AUCTION BUT BEFORE THE INITIAL TERM BEGINS	20
III. BY ENSURING THAT BIDDERS MAINTAIN THEIR OWNERSHIP STRUCTURES, THE COMMISSION CAN IMPROVE THE PROSPECTS FOR GENUINE MINORITY OWNERSHIP	22
CONCLUSION	24
REQUEST FOR EXPEDITED TREATMENT	25

SUMMARY

Throughout half a century of broadcast comparative hearings, the Commission provided for automatic comparative downgrading, commensurate with any downgrading of a diversification showing following a cutoff date. However, it is at best unclear whether new broadcast auction rules prohibit the retention of bidding credits by an entity that downgrades its diversification showing before the auction concludes.

The Commission should clarify its broadcast auction rules to specify that after the Form 175 deadline, an applicant that changes its ownership structure in a manner that would have entitled it to fewer (or no) bidding credits on the Form 175 deadline can retain only those bidding credits that are commensurate with its new ownership structure. Such a clarification would ensure that the value of a bona fide new entrant's bidding credits would not be diluted by bidding credits claimed by those who should not be entitled to them. The requested clarification would particularly benefit minority applicants by relieving them of the risk that those not deserving of bidding credits could deploy the suspect credits to out-finance and outbid them in broadcast auctions. Finally, the requested clarification would ensure that the public would receive the full diversification benefits represented by bidding credits.

Acceptance of an auction password and submission of a bid should constitute affirmative reaffirmation of a bidder's ownership structure and entitlement to bidding credits. If a bidder downgrades comparatively after the filing of Form 175 but before the end of the auction, it should be required to post that fact on the auction website fact at the start of each round of bidding, and thereafter should enjoy only those bidding credits that correspond with its actual structure. Requiring such reports and adjustments to bidding credits would ensure that no bidding credit continues to be deployed after its diversification predicate becomes inoperative. It is a complete and virtually cost-free remedy.

If an auction selectee downgrades comparatively after the auction, but before the start of the initial term that awakens the unjust enrichment rule, it should disgorge to the Treasury the book value of any improvidently deployed bidding credits, plus a substantial "penalty for early withdrawal" of its diversification promise. If the penalty is substantial enough, it will operate prophylactically to ensure that only those who were always capable of building and operating their stations will have an opportunity to do that.*/

---

*/ This Petition reflects the institutional position of MMTC rather than the views of members of the MMTC Executive Committee, Board of Directors, Board of Advisors or Braintrust, or of any individual MMTC member.

The Minority Media and Telecommunications Council ("MMTC") respectfully requests clarification on a matter of profound importance affecting the integrity of broadcast auctions.[1/]

BACKGROUND

On December 5, 2001, the Commission is scheduled to hold an auction ("Auction #37") for 351 new FM construction permits.[2/] These permits comprise the largest group of FM facilities being made available since the 689 Docket 80-90 permits drew their first applications in 1984.

For minorities, the FM auction is supremely important. Ownership concentration, and lack of access to capital have made it increasingly difficult for minorities to enter the industry by buying stations.[3/] Consequently, for many minorities, winning an

---

1/ This petition may be considered under the Commission's duty to act in the public interest. 47 C.F.R. §1.429(b)(3). Alternatively, this Petition may be considered under 47 C.F.R. §1.429(b)(1) and (b)(2) because no party flagged the subtle but critical issue addressed herein until it arose at the Commission's March 7, 2001 Auction #37 workshop. Finally, the Commission may consider this Petition under its general powers, 47 C.F.R. §1.1, or its power to issue declaratory rulings, 47 C.F.R. §1.2. If leave is required to file this Petition, it is respectfully requested.

2/ Auction for FM Broadcast Construction Permits Postponed Until December 5, 2001, Public Notice, Report No. AUC-00-37-G (Auction No. 37), DA 01-619 (released March 7, 2001) ("Auction #37 Postponement") at 1.

3/ See generally K. Ofori et al., Blackout? Media Ownership Concentration and the Future of Black Radio (1997) (documenting how concentration is forcing African Americans out of radio ownership); U.S. Department of Commerce, National Telecommunications and Information Administration, Changes, Challenges, and Charting New Courses: Minority Commercial Broadcast Ownership in the United States (December, 2000) ("NTIA 2000 Minority Ownership Report") at 45-46 (discussing minority broadcasters' endemic difficulties in securing access to capital.)

auctioned construction permit affords the only realistic opportunity to become a station owner.[4/]

4/ When auctions were proposed in 1994, MMTC opposed them because auctions disfavor those without inherited wealth. See Comments of MMTC, NAACP, LULAC and the National Bar Association in GC Docket No. 92-52 (Reexamination of the Policy Statement on Comparative Broadcast Hearings), filed July 29, 1994 at 2 (in light of the "unsurpassed influence" of radio on youth socialization and racial tolerance, "the Commission should not...throw[] up its hands and raffl[e] off the last parcels of broadcast spectrum...Title III radio broadcasting services should not be licensed only to the party with the deepest pockets.")

Assuming auctions were to be used, MMTC advocated race-conscious bidding credits narrowly tailored to remedy the consequences of the Commission's ratification and validation of the past discrimination of its licensees. See Reply Comments of MMTC, PP Docket No. 93-253 (Reexamination of Section 309(j) of the Communications Act - Competitive Bidding), filed October 3, 1994, at 3 ("MMTC Competitive Bidding Comments") (applauding Commission's adoption of a 40% bidding credit and installment payment plan for designated entities for the regional narrowband auctions, and urging that "[i]t is also appropriate for the Commission to adopt additional minority ownership incentives.")

Although the Commission did not adopt a race-conscious plan, it did predict that the new-entrant bidding credits it adopted for broadcast auctions would "promote opportunities by minorities and women consistent with congressional intent without implicating prematurely the constitutional issues" that figured in Adarand v. Peña, 515 U.S. 200 (1995) ("Adarand"). Implementation of Section 309(j) of the Communications Act -- Competitive Bidding for Commercial Broadcast and Instructional Television Fixed Service Licenses (First Report and Order), 13 FCC Rcd 15920, 15995 ¶189 (1998) ("Competitive Bidding First R&O"), recon. granted in part, denied in part on other grounds by Memorandum Opinion and Order, 14 FCC Rcd 8724 (1999), modified in other respects by Memorandum Opinion and Order, 14 FCC Rcd 12541 (1999) ("Competitive Bidding Further MO&O"), affirmed sub nom. Orion Communications Limited v. FCC, D.C. Cir. No. 98-1424 (per curiam), 20 C.R. 784 (released June 13, 2000). See also Omnipoint Corp. v. FCC, 78 F.3d 620 (D.C. Cir. 1996) (holding that FCC acted reasonably in adopting small business-based eligibility rules and abandoning former race conscious rules in order to avoid Adarand challenge.)

Generally, race-neutral programs should be attempted before race-conscious ones are considered. See City of Richmond v. J.A. Croson Co., 488 U.S. 469, 507-510 (1989). Auction #37 will be the first test of the Commission's race-neutral approach to broadcast ownership. MMTC has invested considerable resources into helping this initiative succeed.

Bearing this in mind, on March 1, 2001 MMTC published The MMTC FM Auction Guide and distributed it widely to minority broadcasters. From March 7-9, 2001 at the Department of Commerce, MMTC held a seminar on Auction #37. Fifty minority broadcasters, virtually all of whom were new entrants, attended the MMTC seminar.

Many of MMTC's seminar participants also attended the Commission's March 7, 2001 workshop on Auction #37 regulations and procedures. This Petition is filed to clarify a point raised by a question at the Commission's workshop.

I. THE BROADCAST AUCTION RULES CONTAIN A LOOPHOLE THAT COULD SIGNIFICANTLY DILUTE THE VALUE OF BIDDING CREDITS

The Auction #37 rules specify that an applicant's eligibility for bidding credits, based on the mass media interests of the applicant and those with attributable interests in the applicant, "shall be determined as of the short-form (FCC Form 175) filing deadline[.]"[5/] The question asked at the Commission's workshop was essentially this: suppose, after the Form 175 date, an applicant changes its structure to one that would not have yielded as many bidding credits before the Form 175 date. Will the Commission reduce the applicant's bidding credits? The Commission's staff responded, accurately, that the rules might be ambiguous on that point.

While the broadcast auction rules almost surely prevent the acquisition of new or additional bidding credits after the Form 175

5/ Auction Notice and Filing Requirements for FM Broadcast Construction Permits, Public Notice, Report No. AUC-00-37-C (Auction No. 37), DA 01-119 (released January 19, 2001) at 13 ("Auction #37 Rules"). The Form 175 deadline for Auction #37 is now October 5, 2001. See Auction #37 Postponement at 1.

date,[6] they appear not to clearly require that an applicant must relinquish its credits or face other penalties if it abandoned its Form 175 ownership structure that yielded bidding credits before the auction ends, or after the auction but before the "initial term" whose commencement awakens the unjust enrichment rule, 47 C.F.R. §1.,211(d)(1).[7]

6/ The Auction #37 Rules expressly require divestitures to be consummated before the Form 175 deadline in order to avoid attribution. Id. at 13 and n. 29. While not expressly mentioning a no-upgrade policy, this attribution-avoidance requirement amounts to the same thing because the only manner by which a comparative upgrade could be effectuated under the current definition of bidding credits is through the divestiture of an interest in a medium of mass communications. It is noteworthy that in the wireless auction context, the Commission has had occasion to deny a request for waiver of its general no-upgrade rule, 47 C.F.R. §1.2105(b)(2). Two Way Radio of Carolina, Inc., 14 FCC Rcd 12035, 12043 ¶15 (1999) ("Two Way Radio") (holding that a proposed post-auction upgrade in a wireless applicant's eligibility for treatment as a small business would make it "possible for a bidder to use the amendment process as a mechanism to gain unfair advantage over other bidders in the auction.") Thus, a no-upgrade policy appears safely embraced within the Commission's law of both broadcast and wireless auctions.

7/ Not only do the rules not state that a post-Form 175 comparative downgrade occuring before the auction ends will result in the loss of bidding credits, the rules can easily be read in good faith to mean that the bidding credits would be retained:

First, the Auction #37 Rules specify that an applicant's eligibility for bidding credits, based on interests of the applicant and those with attributable interests in the applicant in other media of mass communications, "shall be determined as of the short-form (FCC Form 175) filing deadline[.]" Auction #37 Rules at 13. The Auction #37 Rules are silent on the treatment of diversification downgrades occurring after Form 175 is filed but before the start of the "initial term" that marks the beginning of the time when the unjust enrichment rule (47 C.F.R. §1.2111(d)(1)) applies. Indeed, the Auction #37 Rules state that after filing Form 175, an applicant may not "change New Entrant Bidding Credit Eligibility[.]" Id. at 18 (emphasis supplied); see also id. at 45 (Guidelines for Completion of FCC Form 175 and Exhibits) ("[a]pplicants are advised that [the Form 175 filing] is the sole opportunity to select 'New Entrant' status and claim a bidding credit level (if applicable). There is no opportunity to change

[n. 7 continued on p. 5]

7/ [continued from p. 4]

the election once the initial short-form filing deadline passes" (emphasis supplied)). The word "change", of course, includes both upgrades and downgrades. Thus, the Commission appears to be telling applicants that their bidding credits will remain intact even if their ownership structures happen to change.

Second, Form 175 requires a certification that the applicant will "remain in compliance with any service-specific qualifications applicable to the licenses on which the applicant intends to bid including, but not limited to, financial qualifications[.]" 47 C.F.R. §1.2105(a)(2)(vii) (emphasis supplied). Since bidding credits are a comparative incentive and not a "qualification," this language appears to inform applicants that they need not "remain in compliance" with the showing that yielded them their bidding credits. The rule's reference to "financial" adds to the inference that the word "qualifications" in the rule has the same essentially literal meaning that it had in the hearing-era phrase "basic qualifications." The broadcast-specific rule, 47 C.F.R. §73.5002(b) and the Auction #37 Rules are silent on whether any additional certifications must be made.

Third, the rules provide that after being filed, Form 175 cannot be amended to reflect "changes in an applicant's size which would affect eligibility for designated entity provisions." 47 C.F.R. §1.2105(b)(2) (emphasis supplied). The Commission referred again to an applicant's "size" in its decision adopting the broadcast auction rules. See Competitive Bidding First R&O, 13 FCC Rcd at 15976 ¶145. That has to have been a mistake; it is apparently an inadvertent carryover from the general auction rules' size-based definition of a small business designated entity. The word "size" is misplaced in a discussion of broadcast auction bidding credits, since they are calculated on the basis of the number and location of media outlets owned, and not on the basis of the "size" of a designated entity. For example, an applicant owning a media outlet in a market containing the community of license of a permit being sought (and thus entitled to no bidding credits) might be smaller in size than an applicant owning a media outlet in a different but larger market (and thus entitled to a 25% bidding credit.) However, even if the references to "size" were intended as an inexact way of referring to any and all changes in media holdings that would affect an applicant's entitlement to bidding credits, the language in the rule prohibiting amendments does not make it clear that those changing their structures to add new media interests after the Form 175 deadline will have their bidding credits adjusted downward. Neither the broadcast-specific rule nor Auction #37 Rules offer a contrary interpretation of §1.2105(b)(2). See 47 C.F.R. §73.5002(c) and Auction #37 Rules at 16.

[n. 7 continued on p. 6]

The Commission seldom construes its own silence or ambiguity to the detriment of a regulatee;[8/] thus, a clarification is in order so the public will be sure what the law is.

7/ [continued from p. 5]

Fourth, Form 301 applications require the applicant to list and summarize agreements "that support the applicant's eligibility as a small business under the applicable designated entity provisions[.]" (emphasis supplied). 47 C.F.R. §1.2112(b)(2)(i); see also FCC Form 301 (May, 1999 version), Section II - Legal, Question 10. However, if "eligibility" is determined as of the Form 175 date, the documents that must be submitted with Form 301 would be the documents that had been in effect on the Form 175 date. The broadcast-specific rule and the Auction #37 Rules drop the "designated entity" terminology but are silent on whether an applicant must report on Form 301 its qualifications for bidding credits as of any date other than as of the Form 175 "eligibility" date. See 47 C.F.R. §73.5005(a) and Auction #37 Rules at 31.

Fifth, the unjust enrichment provision of the rules relating to bidding credits provides only that "within the initial term" a licensee using a bidding credit that seeks "to assign or transfer control of a license to an entity that does not meet the eligibility criteria for a bidding credit" or that "seeks to make any ownership change that would result in the licensee losing eligibility for a bidding credit (or qualifying for a lower bidding credit)" will be required to reimburse the government for the amount of the ineligible bidding credit, plus interest. 47 C.F.R. §1.2111(d)(1). Since this disgorgement is contemplated only if the ownership change occurs "within the initial term", it appears to omit ownership changes that occur at any time between the Form 175 date and the start of the license term. The Commission's decision adopting broadcast auction rules adopts no broadcast-specific rule paralleling §1.2111(d)(1), and the Commission's discussion of this issue simply adopts the "unjust enrichment" formulation in Part I of the rules. See Competitive Bidding First R&O, 13 FCC Rcd at 15997 ¶194. The Auction #37 Rules do not address unjust enrichment.

8/ "[W]here the regulation is not sufficiently clear to warn a party about what is expected of it[,] an agency may not deprive a party of property by imposing civil or criminal liability." General Electric Co. v. EPA, 53 F.3d 1324, 1328-29 (D.C. Cir. 1995), quoted in Trinity Broadcasting of Florida, Inc. v. FCC, 211 F.3d 618, 628 (2000) ("Trinity"). In Trinity, the court vacated the denial of license renewal for an applicant whose ownership structure allegedly conflicted with the Commission's rules. See also Fox Television Stations, Inc., 10 FCC Rcd 8452, on reconsideration, 11 FCC Rcd 5714 (1995) (declining to impose sanctions where an applicant allegedly had evaded the Commission's policies on reporting alien stock ownership interests.)

It would be a mistake to allow an applicant to propose a structure that confers bidding credits, then abandon that structure and still retain the credits or the post-auction benefits flowing from the credits. An applicant taking advantage of such a loophole would receive a considerable transfer of wealth as a reward for having abandoned its ownership structure.

For example, an individual without media interests could initially create a sole proprietorship company and thereby secure a 35% bidding credit on the Form 175 date. On the next day, that person could deliver a substantial interest in her company, and a secure option to acquire the radio station as soon as the rules allow, to a company that holds multiple media interests.[9/] The multimedia company could supply virtually all of the applicant's

---

9/ Actually, these pre-auction restructurings would be most likely to occur at an 11th hour decision point, such as the day before upfront payments are due, the day before the auction, or even during the auction itself. If an applicant restructures on the day before the auction, this scenario might obtain:

October 5, 2001	Individual files Form 175 claiming bidding credits
November 5, 2001	Individual makes upfront payment
December 4, 2001	Individual takes on multimedia partner
December 5, 2001	Auction #37 begins
December 10, 2001	Auction ends
December 11, 2001	Public Notice issued, announcing results
December 12, 2001	Merged entity submits downpayment and files Form 301
December 14, 2001	Form 301 accepted for filing
December 24, 2001	Petitions to Deny due; none filed against merged entity's Form 301
December 28, 2001	Merged entity's Form 301 granted
December 31, 2001	Merged entity commences construction of radio station
January 3, 2002	Merged entity quietly timely files §1.65 report of its merger
January 4, 2002	Losing bidders read §1.65 report but are powerless to seek redress.

[n. 9 continued on p. 8]

financing, and thus usually exercise de facto control, without competitors or the Commission knowing about it.10/ Although the original sole proprietor may have planned this scenario with her future partner well in advance of the lock-in date, no one would ever know that because there is no discovery. Yet even if the sole proprietor had made no such advance plans, she could still be unjustly enriched by absence of an automatic downgrading rule. She could simply raffle off her bidding credits to less diverse entities in what would amount to a private auction. The resulting merged entity, formed only for the unbusinesslike purpose of trumping its competitors, could accurately be characterized by a reviewing court as "strange and unnatural."11/

9/ [continued from p. 7]

Under this scenario, the restructured entity would not be required to notify the Commission of its restructuring (whatever its effect on bidding credit eligibility) until after it had survived the petition to deny deadline, won the permit, and even begun construction. If the restructuring occurred during the auction (as is likely in an auction running longer than the five days in our example above) the restructured entity could deploy the bidding credits to win the auction, survive the petition to deny deadline, obtain a grant, and be testing its transmitter before it would have to file its §1.65 report. Worse yet, if the restructuring occurred after the auction but before the "initial term" that awakens the unjust enrichment rule, the applicant might never be held accountable.

10/ The Commission modified its attribution rules in the auction context, hoping to avoid this very result. Competitive Bidding Further MO&O, 14 FCC Rcd at 12543 ¶6 ("attributing the media interests held by very substantial investors would prevent a large media group owner from providing all the financing for an auction applicant that then claims new entrant status and eligibility for a substantial bidding credit" (fn. omitted)). See also Auction #37 Rules at 14.

11/ This famous phrase was expressed in Bechtel v. FCC, 957 F.2d 873, 880 (D.C. Cir. 1992) ("Bechtel I").

II. THE COMMISSION SHOULD ENSURE THAT NO APPLICANT USES BIDDING CREDITS THE APPLICANT DOES NOT DESERVE

A. THE COMMISSION HAS NEVER BEFORE PERMITTED THE RETENTION OF COMPARATIVE BENEFITS BY APPLICANTS WHOSE STRUCTURES WERE NO LONGER CONGRUENT WITH THEIR COMPARATIVE BENEFITS

The Commission has had a longstanding policy requiring automatic comparative downgrading commensurate with an applicant's reported diversification downgrading. That policy is a corollary to the Commission's even longer-standing policy barring applicants from receiving credit for post-cutoff date comparative upgrading.

The no-upgrade policy is over half a century old.[13/] Most famously articulated in 1970,[14/] it evidently remains in effect in the point system selection process for mutually exclusive reserved channel noncommercial applicants.[15/] It has also been applied in wireless auctions,[16/] and it will apply in broadcast auctions.[17/]

13/ Board Member Norman Blumenthal has dated the no-upgrade policy to Ashbacker Radio Corp. v. FCC, 326 U.S. 327 (1945). See Daytona Broadcasting Company, Inc., 97 FCC2d 212, 216 (1984) ("Daytona"), review granted in part, denied in part, 59 RR2d 1302 (1985).

14/ The most-cited expression of the policy was in Erwin O'Connor Broadcasting Co., 22 FCC2d 140 (Rev. Bd. 1970), which set out six factors to be considered in satisfying the "good cause" criteria for postdesignation amendments. Among those criteria were "that the proposed amendment would not disrupt the orderly conduct of the hearing or necessitate additional hearing; that the other parties will not be unfairly prejudiced, and that the applicant will not gain a competitive advantage." Id. at 143.

15/ See Reexamination of the Comparative Standards for Noncommercial Educational Applicants (Report and Order), 15 FCC Rcd 7386, 7423 ¶90 (2000) (explaining that an applicant's claimed entitlement to comparative points, as set out in its application, is reviewed by Commission to select a permittee, with no provision for amendments to point showings.)

16/ See Two Way Radio, 14 FCC Rcd at 12043 ¶15.

17/ See discussion at p. 4 n. 6 supra.

Like the no-upgrade policy, the automatic downgrade policy is well established in broadcast law.[18/] The automatic downgrade policy serves the same purpose as its parent, the no-upgrade policy: preventing an applicant from gaining an unfair advantage relative to its competitors. Allowing applicants to retain bidding credits for abandoned pre-cutoff date proposals confers an unfair advantage in just the same way that it would confer an unfair advantage to allow applicants to claim additional bidding credits for post-cutoff date proposals.

Applying the automatic downgrade policy to auctions could not be more logical. As noted earlier, its parent of the automatic downgrade policy is the no-upgrade policy, which is already embraced within the Commission's laws of wireless and broadcast auctions.[19/] In the comparative hearing context, the automatic downgrade policy was used to apportion diversification credits; thus, it makes sense to use the same policy to apportion bidding credits in auctions. After all, bidding credits in auctions are the direct policy successors of diversification credits in comparative hearings. The purpose of automatic downgrading in an auction is the same as its purpose in a hearing -- preventing

---

18/ The Board articulated the automatic downgrade policy in Daytona, 97 FCC2d at 218 (holding that when applicants for the same permit merge after the cutoff date, the surviving applicant will inherit the least comparatively advantageous attributes of each of the merging applicants.) Earlier cases applying the automatic downgrade policy include W.S. Butterfield Theatres v. FCC, 237 F.2d 552, 556 (D.C. Cir. 1956) (change in programming and facilities) and Enterprise Co. v. FCC, 231 F.2d 708 (D.C. Cir. 1955), cert. denied, 351 U.S. 920 (1956) (merger). See discussion in Richard P. Bott II, 4 FCC Rcd 4924, 4927 ¶18 (Rev. Bd. 1989), review denied, FCC 90-109 (released April 12, 1990).

19/ See discussion at p. 4 n. 6 supra.

unjust enrichment and thus preserving for the public the benefits of diversification. Whether the permittee is ultimately chosen by a computer or a judge is irrelevant to whether an applicant should be entitled to receive a comparative advantage. Indeed, because the integrity of auctions is based entirely on self-reporting by applicants, the downgrading of credits commensurate with diversification downgrading is needed even more critically in auctions than it was in hearings.20/

In the hearing context, the determination of credits began when the Commission established a date beyond which amendments could not be filed as a matter of right, meaning that as of that date applicants were required to lock in their comparative showings.21/ This date, which in its final incarnation was known

---

20/ In discovery and at trial, comparative hearing applicants had to defend the genuineness of their ownership structures under the watchful eyes of their opponents and a judge. That safeguard is unavailable in auctions, which rely entirely on paper self-reporting. The reliability of self-reporting has only the degree of integrity possessed by the competitor most willing to push the regulatory envelope.

It is true that losing bidders in an auction have every right (and ten days) to file petitions to deny pursuant to 47 C.F.R. §73.5006. However, given the ambiguous status of automatic downgrading in the law of broadcast auctions, an allegation that a bidder used bidding credits to which it may not have been entitled would be unlikely to result in the bidder's disqualification. The Commission would probably have to view such an allegation as comparable to an allegation, in the comparative hearing context, that an applicant's diversification or integration proposal was unreliable. In such a case, diversification or integration credit would have been denied but the applicant would not have been disqualified. See, e.g., Evansville Skywave, Inc., 7 FCC Rcd 1699, 1700-1701 ¶¶15-18 (1992) (holding that a showing of "deceptive or abusive intent" is necessary to sustain the conclusion that an applicant committed disqualifying misconduct.) Having no possibility of supplanting the winning bidder, no rational losing bidder would go to the effort and expense of filing a petition to deny.

21/ See generally Alexander S. Klein, 86 FCC2d 423, 434 (1981).

as the "B-cutoff date," fell promptly after the Commission issued a hearing designation order, and just before discovery was set to begin. While an applicant could change its comparative showing after the B-cutoff date,[22/] such a change in its showing would generally be accepted into the record for reporting purposes only. Thus, the applicant would receive no credit for any comparative upgrading.[23/]

By denying credit for post-B-cutoff comparative upgrades, the Commission prevented applicants from adopting new ownership or operating structures whose only purpose was to appear more attractive than their competitors' comparatively superior showings. Similarly, if an applicant changed its comparative showing to one less advantageous than the showing profferred as of the B-cutoff date, the applicant would be evaluated based on the new, less advantageous showing. In this way, the Commission prevented applicants from being rewarded for comparative attributes that no longer existed. Applicants were thereby disincentivized from falsely promising integration or diversification benefits on the B-cutoff date, secure in the knowledge that they could later

---

22/ Changes in comparative showings must be reported within 30 days. 47 U.S.C. §1.65.

23/ See, e.g., Kennebec Valley Television, Inc., 3 FCC Rcd 4522 ¶4 (1988) (explaining that the Commission would accept, for reporting purposes only, a post-B-cutoff amendment that would result in impermissible comparative upgrading.)

quietly disclaim their promises while still receiving comparative credit for them.[24/]

The no-upgrade/automatic downgrade paradigms were high points of comparative hearing procedure. Although the Court of Appeals has viewed some aspects of the comparative process with skepticism,[25/] it has never had occasion to quarrel with the no-upgrade/automatic downgrade paradigms. These paradigms served the Commission and the public well by preventing widespread structural abuse.

Having quite properly determined to withhold new bidding credits for post-cutoff comparative upgrades in broadcast auctions,[26/] it would seem logical for the Commission to prevent applicants from retaining bidding credits for ownership structures they have abandoned. Bidding credits' value lie in the auction-winning power they deliver to an applicant, relative to

---

24/ Board Member Blumenthal explained in 1984:

> the bar against "upgrading" is indispensable to the assurance of full and fair notice to (actual or potential) competing applicants of the make-up and the potential strength of the proposals of a mutually-exclusive adversary. Broadcast licenses are awarded on the basis of relative competitive merit...and, to be blunt, comparative licensing proceedings conducted under the Policy Statement [1 FCC2d 393 (1965)] are far too exhaustive and expensive to allow an applicant to be drawn deeply into a competition for the license, only to be confronted by a competitor whose comparative position has been improved post hoc by decisionally significant changes in its ownership structure or its broadcast proposals.

Daytona, supra, 97 FCC2d at 216-17.

25/ See, e.g., Bechtel I, supra; Bechtel v. FCC, 10 F.3d 875 (D.C. Cir. 1993) ("Bechtel II").

26/ See discussion at p. 4 n. 6 supra.

applicants lacking them.[27] Thus, allowing a "downgrader" to retain bidding credits for a nonretained ownership structure hurts other applicants' chances as much as allowing an "upgrader" to secure bidding credits by creating a new and possibly nongenuine structure.

Indeed, allowing downgraders to retain their bidding credits would hurt the straight-arrow applicants much more than it would hurt to give upgraders new bidding credits. An upgrader seeks to obtain new bidding credits by proposing to divest media interests, while a downgrader seeks to retain bidding credits while bringing in a media owner that provides a new source of financing. Thus, the upgrader would get bidding credits but would have to carry a divestiture pledge, while the downgrader would get bidding credits and financing too. The downgrader would be much better positioned than the upgrader to prevail over the other applicants.[28]

27/ The economic operation of the tax certificate policy provides a close parallel to bidding credits. A buyer delivering a tax certificate to a seller was seldom able to secure stations at a price discount. The sale typically occurred at almost the same prices that would have obtained in a non-tax-certificate deal; thus, the seller retained the financial benefits of the tax certificate. The tax certificate's real value was that it brought the minority buyer to the dealmaking table. Buyers were able to deploy the tax certificates as a bargaining chip to persuade sellers that it would be at least as desirable to trade with them than with otherwise equivalent potential buyers. See generally E. Krasnow et al., "Maximizing the Benefits of Tax Certificates in Broadcast and Cable Ventures," 13 COMM/ENT Law Journal 753 (Summer, 1991). Similarly, in the auction context, bidding credits may have little effect on the financial exposure of the winning bidder. Instead, bidding credits are likely to assist new entrants in prevailing against other bidders in an auction.

28/ Media companies making post-cutoff date deals to buy bidding credits would be just as culpable as those selling the bidding credits. It is unfair to allow one multimedia company to deploy undeserved bidding credits as an engine of growth while other multimedia companies are limited to market competition as their only engine of growth.

The public, too, would be harmed even more by retained credits for downgraders than by new credits for upgraders. At least an upgrader promises to yield up some diversification in exchange for the new credits; someday, the public might collect on the upgrader's promise. On the other hand, a downgrader retaining its bidding credits, and then selling them in a private auction, would just retain the cash value of the bidding credits, without any obligation to give anything back to the public.

Experience with the Personal Communications Services (PCS) C and F block auctions suggests that there will probably be plenty of litigation over ownership structures in all auctions.[29/] Inherently suspect ownership structures schemes also figured in

---

29/ See, e.g., TPS Utilicom, Inc. Petition to Deny applications of Alaska Native Wireless, L.L.C.,, File Nos. 0000364320 and 0000363827, Auction #35 (filed March 9, 2001) at 2-3 (alleging that when considering applicant's stock on a fully diluted basis, "AT&T exercises de jure control" of the applicant.) As one respected commentator has contended,

> [O]f the 422 [C Block] licenses that were supposed to go to small competitors, 95 percent went to front companies for AT&T, Sprint, Cingular and the other giants....Not only did the giants cheat in order to devour a market set aside for small competitors, but they also used their front companies to qualify for a small-business credit to pay for these licenses, costing us taxpayers $626 million. It's subsidization of monopolization.

Jim Hightower, "Stealing the Cell Phone Market," syndicated column, April 1, 2001.

virtually every comparative hearing.[30/] In a few hearings, judges had to disqualify everyone. Even though hearing applicants faced crossexamination, the FCC Reports and FCC Record are littered with the detritus of dozens of frauds.[31/] Hearings even attracted a number of serial offenders.[32/]

With no opportunities for the examination of witnesses, auctions are likely to attract an even wider cast of envelope-pushers than were drawn to comparative hearings. Human nature being what it is, an unlocked and unattended bank vault makes sinners out of saints. Thus, unless airtight ownership structural integrity protections are designed in, auctions could prove to be even more litigation-prone than hearings.

30/ Judge Williams recited several "startling arrangements manifested just in" the Bechtel case:

> best friends and co-owners of a station swear not to consult with each other; family members with valuable broadcast knowledge and experience agree not to assist the tyro station manager in the family; people with steady jobs and families in one city pledge to leave them and move permanently to another; and wealthy retirees promise to move to and work in small summer towns in Delaware with which they have no former connection.

Bechtel II, 10 F.3d at 886 (quoting Bechtel I).

31/ See Carta Corporation, 5 FCC Rcd 3696, 3701-72 ¶15 (Rev. Bd. 1990) (collecting cases to make the point that "the Commission has been confronted with a large volume of applications that disingenuously depict a two-tier ownership structure so as to exploit artificially the Commission's comparative structure[.]")

32/ See, e.g., Inquiry into Alleged Abuses of the Commission's Processes by Applicants for Broadcast Facilities, 4 FCC Rcd 6342 (1989) (opening Section 403 investigation into Sonrise Management Services, Inc.)

B. RECERTIFICATION OF OWNERSHIP STRUCTURES AT THE START OF THE AUCTION AND DURING EACH ROUND WOULD PREVENT MISUSES OF BIDDING CREDITS BEFORE THE AUCTION ENDS

The Commission can choose from three three potential regulatory mechanisms that could prevent downgraders from benefitting from undeserved bidding credits before the auction ends: (1) reauctioning the permit; (2) requiring disgorgement of the book value of the bidding credits; or (3) requiring bidders to reconfirm their structures and flag decisionally significant structural changes as bids are rendered.[33/] Of these, the third is by far the most desirable approach.

1. Reauctioning. If the Commission waits until after an auction to find out that an applicant downgraded its structure before the auction ended, no relief could make the unsuccessful bidders whole. Denying a Form 301 application or revoking a grant would require a Section 309 hearing and a reauctioning, delaying service to the public and draining resources from the agency.

Nor would reauctioning be fair to the straight-arrow bidder. Such a bidder would derive no consolation from the knowledge that it will have a second opportunity to incur the time and expense of

---

33/ Actually there is a fourth mechanism -- imposing conditions on a grantee. Cf. AirGate Wireless, L.L.C., 14 FCC Rcd 11827, 11835 ¶17 (Chief, Commercial Wireless Division, Wireless Telecommunications Bureau, 1999) (imposing conditions on C and F Block PCS licensee to resolve dispute over whether an applicant was a designated entity at the time it filed its long form application.) However, since this procedure is necessarily ad hoc and situation-specific, it would carry the risk of arbitrariness. It would also consume far more regulatory resources than would a blanket rule, preferably one designed to be prophylactic and usually self-enforcing.

engaging professionals, raising capital, and placing that capital at risk.[34/]

2. Disgorgement. It would not be sufficient for the Commission simply to declare that an applicant that downgrades after filing Form 175, but was not required to (and did not) report that fact until after the auction, must pay the Treasury the book value of the winning bid attributable to the bidding credits, plus interest. Such a remedy seems reasonable in the context of a post-licensing restructuring.[35/] However, pre-licensing disgorgement only of the book value of bidding credits, plus interest, would unjustly enrich the downgrading applicant -- who by then would not even have built the station. The portion of the winning bid attributable to the bidding credits does not come close to representing the entire value of the bidding credits because it does not take into account the value attendant to winning the auction itself and possessing the permit.[36/] To competing

---

34/ That is not the only harm attendant to learning too late that bidding credits were improvidently deployed. If the downgrading applicant lost the auction, the Commission would never know that the applicant had changed its structure and had used bidding credits it did not deserve. Thus, a straight-arrow bidder who won will have paid a premium to outbid the downgrading applicant's undeserved bidding credits. Furthermore, in a simultaneous, multiple-round, ascending auction, other straight-arrow bidders would inevitably have reacted to the undeserving bidder's deployment of bidding credits by focusing, to their detriment, on suboptimal allotments.

35/ The unjust enrichment provision applies only "within the initial term". 47 C.F.R. §1.2111(d)(1). That provision presents no significant risk of abuse. A bidder that wins a license, pays the auction price and builds the station with its own money has assumed all the risks assumed by any other new entrant.

36/ After all; "possession is rather more than nine points of the law." Corporation of Kingston-upon-Hull v. Horner (Lord Mansfield, 1774).

applicants who lost the auction disgorgement would be perceived as little more than a government loan of bidding credits that underwrote the ultimate winner's campaign to outbid them.

3. Recertification. The Commission could simply require that each bidder reaffirm its Form 175 ownership certification a few days before the auction and again at the start of each round of bidding. The Commission can do that by requiring each bidder to affirm, at the time it receives its password, that as of that moment and at each time it submits a bid, it is contemporaneously reaffirming that as of that day its ownership structure has not changed in a manner that would reduce its entitlement to bidding credits. During the auction, if an applicant downgrades its structure so as to reduce its entitlement to bidding credits, it would immediately adjust its bidding credits commensurate with its downgrading, and it would post that fact on the auction website at the start of the next round. In that way, all other bidders will be aware of their competitor's changed circumstances, and would not be subjected to bluffing or other tactics whose success depends on competitors having incorrect information about one another's relative strengths and weaknesses.

Not only would such a requirement be virtually cost free, it would be eminently fair. No revocation hearings would be needed except in instances of deliberate misrepresentations. No auctions would have to be repeated, since bidders could only enjoy bidding credits for so long as they deserved the credits.

This procedure would not only provide complete relief for downgrading, it would actively discourage downgrading and thus promote diversity. The reason is that few if any applicants would

downgrade before the end of the auction if they knew they would lose bidding credits by doing so. Even if they were to overbid, and thus needed to restructure to raise money quickly, it is unlikely that the extent of such an overbidding would come close to the 25% or 35% discounting power of a bidding credit they would stand to lose by restructuring.

C. DISGORGEMENT, WITH A PENALTY FOR EARLY WITHDRAWAL OF A DIVERSIFICATION PROMISE, WOULD PROVIDE AN ADEQUATE REMEDY FOR COMPARATIVE DOWNGRADES AFTER THE AUCTION BUT BEFORE THE INITIAL TERM BEGINS

A challenging scenario is presented by the bidder which enjoys bidding credits and wins an auction -- and then downgrades before the start of the "initial term" that awakens the unjust enrichment rule. Certainly an applicant that never had the interest or ability to build out a permit should not be permitted to restructure itself, disgorge only the book value of the bidding credits, and thereby make a nice but undeserved profit -- a profit that should have gone to a bidder that was always ready and able to build and operate the station. Unfortunately, the rules currently provide no remedy at all in this scenario.[37/]

Owing to the cost to all concerned in time, money and foregone opportunity, reauctioning would provide no remedy at all for downgrades after an auction but before the initial term begins. While recertification works very well as a remedy for downgrades occuring before an auction ends, recertification loses its regulatory power the instant the auction is gavelled to a close. At that moment, the wrong winner has been chosen and the deserving bidder has lost.

37/ See p. 6 n. 7 ¶5 supra.

Disgorgement of the portion of the winning bid attributable to the bidding credits, plus interest, would only provide a partial remedy for downgrades after an auction but before the initial term begins. As in the case of downgrades before or during an auction, disgorgement only of the bidding credits' book value might only serve to commemorate that the Commission had granted the applicant a de facto loan equal to the book value of the bidding credits. The enterprise value attendant to winning the permit would still escape recapture.

Consequently, disgorgement would provide an adequate remedy for post-auction, pre-initial-term downgrades only if they include a very substantial "penalty for early withdrawal" of a diversification promise. A high enough penalty would prophylactically discourage applicants from submitting bids for facilities they know they cannot built out.[38/] While the determination of the amount of such a penalty is unavoidably somewhat arbitrary, it would not appear unreasonable, in the first

---

38/ Following Congress' lead, the Commission has always sought to design its auctions so as to build in deterrence of structural abuse. As the Commission noted when it promulgated its first auction regulations,

> The legislative history suggests that in the auction context Congress's directive to take steps to prevent unjust enrichment was similarly intended to prevent auction winners from acquiring licenses for less than true market value at auction and then transferring them for a large profit prior to providing service....The acquisition of a license through an effectively conducted cmompetitive bidding process is in itself a strong deterrent to unjust enrichment.

Implementation of Section 309(j) of the Communications Act - Competitive Bidding, 9 FCC Rcd 2348, 2385 ¶212 (1994) (fn. omitted) (discussing H.R. Rep. No. 111, 103d Cong., 1st Sess. 253, 257 (1993)).

few auctions, to require downgraders to disgorge a total sum that is double the book value of the undeserved bidding credits.

III. BY ENSURING THAT BIDDERS MAINTAIN THEIR OWNERSHIP STRUCTURES, THE COMMISSION CAN IMPROVE THE PROSPECTS FOR GENUINE MINORITY OWNERSHIP

By ensuring congruence between bidding credits and the public benefit they represent, the Commission would achieve three worthwhile goals.

First, the Commission would ensure that the relative value of a bidding credit is not diluted by the inclusion of undeserved credits in the auction financing pool. If bidding credits can be retained even if an applicant downgrades its structure, almost every applicant will claim a 35% bidding credit. Were that to happen, bidding credits would lose virtually all of their diversification-promoting power. By preventing that outcome, the Commission would be faithful to Congress' expectation that the Commission use bidding credits or similar methods to promote competition and diversity.[39/]

Second, the Commission would preserve new entrants' access to the limited pool of auction-friendly capital. Capital follows bidding credits when they have competitive value; dilution of bidding credits drives capital away. Furthermore, when a downgrader essentially sells its bidding credits to a multimedia company, the cash delivered in return will artificially inflate the bid prices irrespective of how much other applicants' bidding credits have been diluted. Thus, by preventing the dilution of deserved bidding credits with undeserved ones, the Commission would

---

39/ 47 U.S.C. §309(j)(4) (1996). See FCC Report to Congress on Spectrum Auctions, 13 FCC Rcd 9601, 9629 (1997).

help minorities overcome the unique challenges they face in accessing capital for startup ventures.

Third, the Commission would ensure that the public receives the diversification benefits represented by the public wealth embedded in the bidding credits. In particular, closing any loopholes in the structural rules would help prevent any recurrence of the unfortunate events that led to the loss of the tax certificate policy and other pro-diversity measures.40/

Seven years ago, MMTC observed that "abuses of the Commission's processes reduce opportunities for legitimate minority entrepreneurs, and risk tainting a worthwhile program intended to promote diversity and create economic opportunity for minorities and women."41/ Today, minority new entrants' business plans place great confidence in the undiluted value of bidding credits. MMTC has been privileged to know dozens of the minority potential applicants in Auction #37. Virtually all of them are new entrants, or they own only one or two stations. Almost all of them should be entitled to bidding credits. These entrepreneurs look to the Commission for steadfastness and resolve in preserving and promoting diversity and inclusion.

40/ In 1995, exaggerated allegations of structural abuse figured heavily in Congress' decision to eliminate the tax certificate policy. Even before that, in 1993, the Court of Appeals' second Bechtel decision made it virtually impossible for the Commission to continue with comparative hearings. In the end, it mattered little that, for all their flaws, comparative hearings had been quite successful in enabling minorities to start new broadcast stations.

41/ MMTC Competitive Bidding Comments, supra, at 4.

CONCLUSION

For the reasons set out above, MMTC respectfully requests the Commission to clarify its broadcast auction rules as follows:

1. After the Form 175 deadline, an applicant that changes its ownership structure in a manner that would have entitled it to fewer (or no) bidding credits on the Form 175 deadline can retain only those bidding credits that are commensurate with its new ownership structure.

2. Acceptance of an auction password and submission of a bid will constitute affirmative reaffirmation of a bidder's ownership structure and entitlement to bidding credits. If a bidder downgrades comparatively after the filing of Form 175 but before the end of the auction, it will be required to post that fact on the auction website fact at the start of each round of bidding, and thereafter will enjoy only those bidding credits that correspond with its actual structure.

3. If an auction selectee downgrades comparatively after the auction, but before the start of the initial term that awakens the unjust enrichment rule, it should disgorge to the Treasury the book value of any improvidently deployed bidding credits, plus a substantial "penalty for early withdrawal" of its diversification promise. The total disgorgement might equal a sum that is double the book value of the undeserved bidding credits.

REQUEST FOR EXPEDITED TREATMENT

The Form 175 deadline for Auction #37 falls on October 5, 2001. The Commission's decision on this Petition could influence potential applicants' decisions on whether to participate in the auction, and on how to finance their bids. Minority entrepreneurs' difficulties in rapidly securing access to capital have been well documented.[42/] Consequently, in order to allow enough lead time for potential applicants, including minorities, to absorb and react to the Commission's decision on this Petition, the Commission is respectfully requested to rule on an expedited basis.[43/]

Respectfully submitted,

David Honig
Executive Director
Minority Media and
Telecommunications Council
3636 16th Street N.W.
Suite BG-54
Washington, D.C. 20010
(202) 332-7005
mmtcbg54@aol.com

April 19, 2001

42/ See, e.g., NTIA 2000 Minority Ownership Report at 45-46.

43/ MMTC recognizes with appreciation the helpful suggestions of Erwin Krasnow, Esq., Raymond Quianzon, Esq. and S. Jenell Trigg, Esq., and the editorial assistance of MMTC law clerk Carol Westmoreland.