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HEARINGS BEFORE THE SENATE COMMERCE COMMITTEE  
SUBCOMMITTEE ON COMMUNICATIONS  
HELD SEPTEMBER 15, 1989

THE EVOLUTION OF DISTRESS SALES:  
A Direct Benefit to Non-Minorities

by J. Clay Smith, Jr. Esq.  
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Lisa C. Wilson, Esq.

ON BEHALF OF NATIONAL BAR ASSOCIATION<sup>1/</sup>

I. INTRODUCTION

It is a pleasure to be here today before the Senate Subcommittee on Communications to discuss the state of minority ownership of broadcast facilities. A public discussion of this topic is quite timely in light of the recent decisions by the D.C. Circuit dealing directly with the validity of the FCC's minority enhancement policy and the FCC's distress sale policy.<sup>2/</sup>

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<sup>1/</sup> National Bar Association was founded in 1925, and is an organization comprised of Black lawyers across the United States. The National Bar Association has, for the last forty years, actively participated in the formation of the nation's telecommunications policy. J. Clay Smith, Jr., Esq. is currently a Professor of Law at Howard University School of Law in Washington, D.C. Erroll D. Brown, Esq. is currently an associate at O'Malley, Miles and Harrell in Landover, Maryland. Cynthia Mabry, Esq. is currently an associate at Crowell and Moring in Washington, D.C. Lisa C. Wilson, Esq. is currently an associate at Fisher, Wayland, Cooper and Leader in Washington, D.C. All views expressed are those of the authors and of the National Bar Association, and do not express the views of the authors' respective employers.

<sup>2/</sup> See Winter Park Communications, Inc. v. FCC, No. 88-1755 (D.C. Cir. April 21, 1989) (held, awarding qualitative enhancement credit to broadcast applicants that have minority ownership does not violate the equal protection clause of the Fifth Amendment); Shurberg Broadcasting of Hartford, Inc. v. FCC, No. 84-1600 (D.C. Circuit, March 31, 1989) (held, distress sale policy violates Fifth Amendment (continued...))

As many of you are already aware, there has been, and there continues to be a dearth of minority owners of broadcast facilities.<sup>3/</sup> The FCC recognized this fact in 1977 when Republican-appointed FCC Chairman Richard Wiley and Commissioner Benjamin Hooks held the first FCC Conference of Minority Ownership. This historical conference brought to the forefront a host of government officials, broadcasters and lawyers,<sup>4/</sup> and addressed the concern that minorities were not fairly represented in the broadcast marketplace. However, more importantly, the

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2/(...continued)

because program not narrowly tailored to remedy past discrimination or to promote program diversity).

3/ According to the Department of Minority and Special Services of the National Association of Broadcasters, the percentage of minority-owned broadcast facilities was 2.1% in 1986; only 1.45% of those facilities was Black-owned.

4/ FCC MINORITY OWNERSHIP TASK FORCE, CONFERENCE ON MINORITY OWNERSHIP IN BROADCASTING held April 25 and 26, 1977. (hereinafter referred to as "Conference") The Conference examined the reasons for the underrepresentation of minority owners, and explored ways to increase the number of minority owners. The conference brought together such persons as broadcasters Ragan Henry of Broadcast Enterprises, Skip Finley of Sheridan Broadcasting, Inc., Cathy Hughes formerly with WHUR-FM and now owner of WOL-AM, Washington, D.C., and Rene Anselmo with Spanish International Network; numerous government officials such as J. Clay Smith, Jr. then-Associate General Counsel at the FCC, Norman Blumenthal, then-Assistant General Counsel at the FCC, Roy Stewart, then-Chief of the Assignment and Transfer Branch, and Roderick Porter, then-Legal Assistant to FCC Chairman Richard Wiley; and other industry activists including Herbert Wilkins of Syndicated Communications, Inc., Curtis White, broadcast attorney, Harry Shooshan, then with the House Subcommittee on Telecommunications, Erwin Krasnow, then-General Counsel with the National Association of Broadcasters, Patti Grace, then-Community Affairs Director at the National Association of Broadcasters, Dr. Gloria Walker, Dean, School of Communications Clark College, Atlanta, Georgia, and Dr. Lionel Barrow, Dean, School of Communications, Howard University, Washington, D.C.

Conference inspired new Commission policies that aimed to balance the scales of representation for minorities.

In May, 1978, the Commission issued a "Policy Statement on Minority Ownership of Broadcast Facilities."<sup>5/</sup> In the Policy Statement, the Commission acknowledged the minority enhancement credit provision espoused by the D.C. Circuit in two cases, TV-9 v. FCC and Garrett v. FCC <sup>6/</sup>, and further stated that minority applicants engaged in broadcast hearings should be "afforded comparative merit...for construction permits where minority owners were to participate in the operation of the station."<sup>7/</sup> However, because of the "continuation of the extreme disparity between representation of minorities in the population, and those in the broadcasting industry, ...further...action [was required]."<sup>8/</sup> These two cases were the impetus for the Commission's policies aimed at closing the representational gap. These policies are the distress sale policy, and the tax certificate policy. Because of the D.C. Circuit's recent

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<sup>5/</sup> See, Policy Statement, 42 RR 2d 1689 (1978) (hereinafter referred to as "Policy Statement")

<sup>6/</sup> See, TV-9 v. FCC. 495 F.2d 929 (D.C. Cir. 1973) (held, it is consistent with maximum diversification of ownership for FCC in comparative license proceedings to afford enhancement credit to an applicant who, not as mere token, but in good faith as broadening community representation, gives local minority group media entrepreneurship); Garrett Broadcasting Service v. FCC, 513 F.2d 1056 (D.C. Cir. 1975) (held, Black ownership and participation together are likely to bring about programming that is responsive to the needs of the Black citizenry, and this "reasonable expectation" without "advance demonstration", gives it relevance).

<sup>7/</sup> Policy Statement at 1694.

<sup>8/</sup> Id.

decision to invalidate the distress sale policy on the grounds that it violates the Fifth Amendment's equal protection clause of the U.S. Constitution, these comments will focus specifically on this policy alone.<sup>9/</sup>

## II. ORIGIN OF DISTRESS SALE POLICY

There has traditionally been an exception to establish Commission policy against approval of an application for assignment of license when there lies a question concerning the character qualifications of the licensee. In other words, there is precedent for permitting distress sales on various grounds. See, Radio San Juan, Inc., 45 FCC 2d 375 (1974) For example, the Commission has authorized the transfer of a license to a qualified assignee where the licensee has been adjudicated as bankrupt, the individuals charged with misconduct are disassociated from station operations and will derive no benefit from the proposed transfer, and where non-renewal would result in substantial harm to innocent creditors. See, Arthur A. Cirilli, 6 RR 2d 903 (1966); and Twelve Seventy, Inc., 2 FCC 2d 973 (1966).

Historically, the Commission permits distress sales when the licensee is either bankrupt or physically or mentally disabled. In those limited circumstances, the Commission has called the requests Petitions for Special Relief; the name "distress sales"

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<sup>9/</sup> For a legal analysis of the FCC's minority and gender enhancement policy, see, Wilson, "MINORITY AND GENDER ENHANCEMENTS: A Necessary and Valid Means to Achieve Diversity in the Broadcast Marketplace," 40 Fed. Comm. L.J. 89 (1988).

does not appear in Commission opinions until the development of Policy Statement, supra. However, the underlying principle and the procedure for effectuating Petitions for Special Relief and distress sales are essentially the same.<sup>10/</sup>

The Commission in using its equitable powers determined that when the hearing process would cause great hardship for the licensee and granting an exemption would produce only a slight reduction in the deterrent effect, renewals and assignments could be granted without a hearing despite the presence of unresolved issues concerning the character of the licensee. The typical case in which this type of situation arose was where renewal applications had been designated for hearing, the licensees suffered from physical disability which had either contributed to their alleged wrongdoing or caused the proposed hearing to be unusually burdensome for them.<sup>11/</sup>

The Commission has also used its equitable powers in permitting distress sales in certain bankruptcy cases to protect those, such as the creditors of a bankrupt licensee, likely to sustain harm from the license renewal process. Under such circumstances, the Commission would insist that the licensee

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<sup>10/</sup> In the more recent distress sale cases, the Commission has used the term "Petition for Approval of Settlement Agreement." However, the procedure and analysis has remained constant throughout the various types of aforementioned cases.

<sup>11/</sup> See, Tinker, Inc., 8 FCC 2d 22 (1967) (held licensee's heart condition prevents his preparation for, and participation in, the hearing); Martin R. Kariq, 3 RR 2d 669 (1964) (held, congenial fused spine of licensee justified approval of transfer to aid disabled owner to support himself and family.)

agree to retire from broadcasting and reap no profit from the sale of the station. The bankruptcy exception increased the possibility of further departures from the renewal process by using benefit to others -- as opposed to harm to the licensee as the determinative criterion. The Commission also emphasized that a licensee not be given "a profitable escape route from the consequences of his wrongdoing."<sup>12/</sup> The underlying policy which the Commission has applied in cases involving licensees in bankruptcy or receivership is that assignment will not be permitted where there are pending issues concerning a licensee's character qualifications, unless there is a showing that alleged wrongdoers will not benefit from the sale or will derive only a minor benefit which is outweighed by the equities in favor of innocent creditors. See e.g., Second Thursday Corporation, 22 FCC 2d 515 (1970), recon. granted, 25 FCC 2d 112 (1970). In so doing, the Commission has said that a licensee's insolvency and the protection of innocent creditors require a careful ad hoc balancing of competing interests in determining whether or not the Commission should authorize the assignment of a license in the face of the unresolved character issues. See, Erwin A. LaRose and Jimmy Lee Swaggart v. FCC, 494 F.2d 1145 (D.C. Cir. 1974).

Over the years, the Commission has carved out other exceptions to the policy against approval of an application for assignment of license when a question exists concerning the

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<sup>12/</sup> Federal Broadcasting System, Inc., 60 FCC 2d 1036, 1040 (1976).

character qualifications of the licensee's principals. In Martin R. Karig, 3 RR 2d 669 (1964), the Commission permitted permittee Karig to assign his permit because of his physical disability even after an initial decision revoking a construction permit on character qualifications ground. The Commission's reasoning hinged, in large part, on the fact that Mr. Karig would not be able to educate his four children, and was giving up his only ownership interest in broadcasting and would receive no profit from the sale.

In another case, the Commission terminated a renewal hearing where the controlling owner had pleaded guilty to filing false and misleading statements with the S.E.C., had paid \$3,000,000 in damages in a suit for fraudulent exchange of stock, and had pending criminal charges for five counts of committing perjury before a federal Grand Jury. See, Victor Muscat, 33 FCC 2d 568 (1972). In so doing, the Commission did not identify, per se, any mitigating circumstances. Id. at 569.

In WMOZ, Inc., 7 RR 2d 373 (1966), the Commission permitted assignment of a station even after a finding that the licensee was unqualified to be a licensee, and stated "[w]e are vested with a broad discretion in our choices of remedies and sanctions," Id. at 375, and thus it would allow the transfer because of alleged ill health. (Cf. Lorain Journal Co. v FCC, 351 F.2d 824 (1965) (held, Commission has broad discretion to determine choice of sanctions and remedies).

In Twelve Seventy, Inc., 2 FCC 2d 973 (1966), the Commission allowed assignment after hearing, notwithstanding unanswered



questions about benefits to past stockholders. In Radio San Juan, Inc., supra, there were outstanding issues that ordinarily would necessitate an evidentiary hearing, yet the Commission permitted assignment because the licensee "represented that it wants to expeditiously withdraw from broadcasting." Id. at 607-8.

In Hertz Broadcasting of Birmingham, Inc., 57 FCC 2d 183 (1976), there was a pending renewal hearing for, among other things, misrepresentations. The Commission permitted the assignment of WENN and WENN-FM by the receiver of the bankrupt licensee, in spite of the fact, that the assignment would benefit the licensee's sole shareholder, Mr. Hertz, by reducing his debts.

As noted by former Commissioner Benjamin Hooks nearly fifteen (15) years ago, "in none of the foregoing cases, which I presume represent the "exceptional circumstances" to which the majority adverts, are the public interest arguments... compelling." Northwestern Indiana Broadcasting, Corp., 60 FCC 2d 205 (1976).

In his dissenting opinion, Commissioner Hooks referred to the reason cited by the Commission for carving out exceptions to the distress sale policy. As the Commission explained: "that [it is a] rare situation in which the Commission has terminated a hearing without resolving the [outstanding] issues...[although] repeatedly [making] it clear that a hearing will not be terminated without resolving issues to determine basic qualifications, barring exceptional circumstances affecting the

thereafter, the Commission issued a Policy Statement endorsing a commitment to increasing significantly minority ownership of broadcast facilities.<sup>15/</sup> Steps taken by the Commission to implement its policy included an exception to the distress sales policy for minority buyers. Id.

### III. MINORITY STATUS AS EXTENSION OF DISTRESS SALE POLICY

It was not until the year 1978 that the minority factor came into play. When the Commission announced its extension of this existing policy in the Policy Statement, it specifically stated that "grants of distress sales [would be] authorized in circumstances to those now obtaining except that the minority ownership interests in the prospective purchaser [would] be a significant factor." <sup>16/</sup> Thus, the 1978 policy was intended to be utilized in essentially the same manner as when the licensee is either bankrupt or physically or mentally disabled.<sup>17/</sup>

### IV. USE OF DISTRESS SALES AFTER 1978

The Commission's most celebrated use of distress sales, or at least in authorizing "Petitions for Special Relief," involved RKO General Inc., the former licensee of 14 radio and television stations in major markets across the country. The Commission's

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<sup>15/</sup> See, Policy Statement, supra.

<sup>16/</sup> See, Policy Statement at 1695.

<sup>17/</sup> Id. A few months after the Policy Statement was released, the Commission established a minority buyer's listing whereby the FCC maintained a list of minority persons interested in purchasing broadcast facilities, and who wished to make their interests known to sellers, brokers, and other persons who were looking for station buyers. See, Establishment of a Minority Buyer's Listing, 69 FCC 2d 1553 (1978).

licensee." Northwestern, supra, 60 FCC 2d at 210. By way of illustration, the Commission pointed out situations where the licensee is in receivership, where the wrongdoer could not benefit from a grant conditioned upon assignment of the license to a qualified applicant, and where only innocent creditors would otherwise suffer, and the respective hearing has been terminated without resolving qualifications questions. Similarly, the Commission pointed out that unusual circumstances, such as a disabling mental disease, has been considered as a pertinent factor in a licensee's capability to meet its responsibility. Catheryn C. Murphy, 42 FCC 2d 346 (1973); see Walton Broadcasting Co., 28 FCC 2d 111 (1971) and cases cited therein.

In 1976, the executive branch petitioned the Commission to establish a minority ownership policy.<sup>13/</sup> The administration's proposal suggested that "the Commission permit sales of reduced prices of stations designated for license renewal or revocation hearings to groups of at least 50 percent minority ownership." Id. Following in the footsteps of the executive branch, the Commission held a Conference on minority ownership.<sup>14/</sup> Soon

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<sup>13/</sup> BROADCASTING MAGAZINE (February 6, 1978) "The Carter Plan To Get Minorities Into Ownership Of Broadcast, Cable," at p. 47. A White House statement issued at the Tuesday morning announcement of the program said "because of telecommunications' vital role in social, economic and political progress, full minority participation is a critical component of President Carter's economic and social goals... Minority ownership markedly serves the public interest, for it insures the sustained and increased sensitivity to minority audiences."

<sup>14/</sup> See, Conference, supra, at 2.