No. 01-653

In the Supreme Court of the United States

FEDERAL COMMUNICATIONS COMMISSION, PETITIONER

v.

NEXTWAVE PERSONAL COMMUNICATIONS INC. AND
NEXTWAVE POWER PARTNERS INC.

*ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT*

**REPLY BRIEF FOR THE
FEDERAL COMMUNICATIONS COMMISSION**

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TABLE OF AUTHORITIES

REPLY BRIEF FOR THE FEDERAL COMMUNICATIONS COMMISSION

Respondents' brief in opposition fails to come to grips with the critical issue in this case—whether the assignment and regulation of radio spectrum licenses will be governed by communications law and the federal agency to which Congress assigned that responsibility, or by federal courts employing bankruptcy rules and policies designed to regulate debtor-creditor relationships. The Second Circuit correctly concluded that communications law should govern the fundamentally regulatory issue of spectrum license allocation. By contrast, in the decision below, the D.C. Circuit held that bankruptcy law precludes the FCC from enforcing regulatory license conditions. In so doing, the D.C. Circuit inappropriately injected the Bankruptcy Code into the heart of spectrum allocation decisions and, contrary to the Second Circuit, effectively awarded to respondents licenses valued at over $15 billion, despite the FCC's judgment that doing so would disserve the public interest. That erroneous decision clearly warrants further review.

1. By enacting 47 U.S.C. 309(j), Congress required the FCC to employ a market-based system of spectrum allocation—auctions—so that scarce radio spectrum would be licensed to the applicant best able to use it effectively and efficiently in the public interest, as demonstrated by the applicant's willingness and ability to pay more for it than others. As the Second Circuit recognized, that auction mechanism can achieve the goal of "fair and efficient allocation of spectrum licenses * * * *only if* the bids constitute a reliable index of the bidders' commitments to exploit and make the most of the license," *i.e.*, "*only if* the high bid entails the obligation *to make good* the amount bid." Pet. App. 246a (emphases added). For that reason, the Second Circuit concluded that respondents' failure to meet their bid obligations had "more than financial implications." *Id.* at 234a. "It indicated that under the predictive mechanism created by Congress to guide the FCC," respondents were

"not the applicant[s] most likely to use the [l]icenses efficiently for the benefit of the public." *Ibid.*

Neither the D.C. Circuit nor respondents dispute the Second Circuit's conclusion that the payment condition of respondents' licenses is regulatory in nature. Nonetheless, the D.C. Circuit held that Section 525(a) of the Bankruptcy Code bars the FCC from enforcing that condition. That holding threatens to render the most important consideration in licensee selection—the applicants' willingness to pay more than others for the licenses—the least enforceable. See Pet. 16-20. In addition, by holding that the FCC cannot cancel licenses for nonpayment of winning bids, the decision below prevents the FCC from using installment payments without leaving "its regulatory actions open to attack under Chapter 11 of the Bankruptcy Code." Pet. App. 49a. In enacting Section 309(j), however, Congress specifically endorsed "installment payments" as a method of "promoting economic opportunity and competition," encouraging participation by smaller and disadvantaged entities, and "avoiding excessive concentration of licenses." 47 U.S.C. 309(j)(4) and (j)(3)(B). The D.C. Circuit's decision takes that congressionally sanctioned tool away from the Commission. Pet. 18.

The effect of the D.C. Circuit's decision has already been substantial. Dozens of licensees that acquired spectrum through the auction process have filed for bankruptcy protection and now regularly invoke the decision below to retain their licenses despite failing to meet regulatory payment obligations.[1] For example, 29 related entities in California recently filed an adversary proceeding in their Chapter 11 cases after failing to make installment payments on licenses valued at about $10 million. *In-Sync Interactive/Monterey, Inc.* v. *FCC*, No. LA 01-42617-ES (Bankr. C.D. Cal. Dec. 10, 2001). Relying on the D.C. Circuit's decision, the amended complaint (at ¶ 45) contends that Section 525 "prevents the termination of [the] licenses." The D.C. Circuit's decision

[1] We are advised that, to date, the holders of 337 licenses, with payment obligations of $6.9 billion, have declared bankruptcy.

also has been invoked in a Tenth Circuit case concerning the FCC's cancellation of another bankrupt bidder's C-Block licenses. See, *e.g.*, Appellant's Reply Br. at 8-11, *United States* v. *Kansas Pers. Comm. Servs., Ltd.*, No. 01-3042 (argued Jan. 17, 2002). Absent further review, the D.C. Circuit's decision *in this case alone* will require the FCC to award respondents licenses valued at over $15 billion, even though respondents demonstrated their inability or unwillingness to pay—and insisted initially that they should pay no more than one quarter of—the $4.7 billion they bid at auction. Respondents' stated willingness and ability to pay, of course, was the principal reason for awarding them the licenses over other applicants. See Pet. 7-8, 16.

After twice seeking this Court's review of earlier decisions in this controversy, respondents now insist that the question presented lacks importance because the Commission no longer provides for installment payments in license auctions. Br. in Opp. 16. But it is self-evident that a decision creating a massive loophole in a regulatory regime is more important than one keeping it shut. The issue is already arising with increasing frequency, as others rush to take advantage of the decision below. See pp. 2-3, *supra*. Moreover, the Commission suspended its use of installment payments precisely because of the delay and uncertainty created by bankruptcy litigation. As the Commission explained, its change in policy was prompted by the harm to the public interest that results "when licenses are held in abeyance in bankruptcy court." *In re Amendment of the Commission's Rules Regarding Installment Payment Financing for PCS Licensees*, 13 FCC Rcd 15,743, ¶ 50 (1998); Pet. 19 n.5. In this case, for example, respondents have held some of the most valuable spectrum in the nation for five years, but have spent most of that time restructuring in bankruptcy. As a result, they have yet to provide service to a single customer.[2]

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[2] Refusing to accept responsibility for their default, respondents suggest that the *Commission* caused their bankruptcy by "flooding the spectrum market" with licenses after respondents submitted their bids. Br. in

The effect of the decision below, in any event, is not necessarily limited to installment payments. Section 525 declares not only that an agency cannot "revoke" or "suspend" a license solely for nonpayment of a dischargeable debt, but also that an agency cannot "deny" a license for that reason. 11 U.S.C. 525(a). Because there is a necessary (and sometimes substantial) period of time between the close of an auction and license awards, Pet. App. 217a; Pet. 19 n.6, even applicants that must pay in full on the license's issuance may declare bankruptcy following the auction but before receiving the license. Relying on the decision below, such applicants can now argue that Section 525 prohibits the Commission from denying (as well as revoking) a license for failure to satisfy a winning bid.[3] The decision thus threatens to render unenforceable the condition—willingness and ability to pay—that is most critical in identifying the applicant that will best use the spectrum in the public interest, even where lump-sum payments are required.

Opp. 2. Not so. The additional auctions were planned and announced publicly in August 1995, well before respondents submitted their winning bids. Pet. App. 308a.

[3] Respondents contend that, under those circumstances, the agreement between the high bidder and the FCC would constitute an "executory contract." If the bidder opted to "assume" the contract, they argue, the debt would become a post-petition obligation that is not "dischargeable" in bankruptcy and thus outside of Section 525's protections. Br. in Opp. 17 & n.8. Respondents cite no case holding that executory contracts are excepted from Section 525, and the contention has been rejected by numerous courts. See, *e.g.*, *Curry* v. *Metropolitan Dade County*, 148 B.R. 966, 972 (S.D. Fla. 1992); *Stoltz* v. *Brattleboro Hous. Auth.*, 259 B.R. 255 (D. Vt. 2001). Moreover, under respondents' theory, their payment obligations also would be non-dischargeable, because their licenses also would be executory in nature. While respondents must obey FCC rules, the FCC must protect respondents' exclusive right to the spectrum. See *Fenix Cattle Co.* v. *Silver*, 625 F.2d 290, 292 (9th Cir. 1980). In any event, like the hypothetical bidder who assumes an executory contract, respondents cannot both retain their licenses and alter in bankruptcy the payment obligations contained in those licenses, as the Second Circuit recognized. See pp. 6-7, *infra*. Respondents' payment obligations are thus no more dischargeable than obligations arising from assumed executory contracts.

Respondents' claim that the FCC can avoid the impact of the decision below by canceling licenses based on an "array of" factors other than nonpayment, Br. in Opp. 18; see also *id.* at 15, is contrary to statutory policy. The submission and fulfillment of the winning bid are the means by which the Commission identifies the applicant that will best use the licenses in the public interest. Pet. App. 234a; Pet. 8, 9-10, 14-16. It was precisely to avoid hearings and multi-factor considerations, with the attendant uncertainty and delays, that Congress instituted market-based auctions. H.R. Rep. No. 111, 103d Cong., 1st. Sess. 248 (1993); Pet. 2-3, 20 n.8.

Finally, respondents suggest that the parties' willingness to enter into a contingent settlement agreement shows that the case lacks importance. Br. in Opp. 15. Respondents' reliance on the failed settlement agreement is of dubious propriety. Cf. Fed. R. Evid. 408. Besides, the settlement—which prompted the Attorney General to transmit legislation to Congress and the Chairman of the FCC personally to testify before Congress—only underscores the fiscal, administrative, and legal significance of this issue. The Attorney General and FCC Chairman, moreover, advised Congress that the proposed settlement left the FCC's auction process subject to attack under the D.C. Circuit's decision and that, as a result, a decision of this Court or separate corrective legislation would be required "to protect the auction process."[4] And it is not without significance that the settlement

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[4] Statement of FCC Chairman Michael K. Powell, Before the Subcomm. on Telecomm. and the Internet of the House Comm. on Energy and Comm. on the NextWave Settlement Legislation 2 (Dec. 11, 2001); Letter from Attorney General John Ashcroft to Hon. Richard B. Cheney at 1-2 (Nov. 28, 2001) (similar). Respondents further mischaracterize the record when they state (Br. in Opp. 15-16) that the FCC permitted another C-Block bidder, Pocket Communications, to retain licenses for only 63% of its bid. In fact, DCR PCS, Inc., a subsidiary of Pocket Communications, adopted one of the restructuring options offered by the Commission and thus will pay in full for any licenses it retains. See 14 FCC Rcd 1817 (1998); *In re Amendment of the Commission's Rules Regarding Installment Payment Financing for PCS Licensees*, 13 FCC Rcd 8345, ¶ 20 (1998); Pet. 6-7. Respondents did not elect any of those restructuring

foundered for lack of congressional approval amid criticism by lawmakers that "the government can no longer afford to simply 'pay off' a company whose only contribution to the American economy has been to manipulate, for private gain, the results of an improperly designed auction of a valuable public good." Letter from Sen. John McCain to Sen. Tom Daschle and Sen. Trent Lott 2 (Oct. 26, 2001).

2. The D.C. Circuit ruled that Section 525 prohibits the FCC from canceling respondents' licenses for failure to satisfy regulatory bid obligations, because those obligations constitute debts that are "dischargeable" in bankruptcy. Pet. App. 41a-44a. In contrast, the Second Circuit ruled that the FCC's timely payment requirement, like its full payment requirement, is a regulatory condition that lies beyond the bankruptcy court's power to "alter[] or impede[]." Pet. App. 119a-120a. See also *id.* at 236a-237a & n.11, 245a n.15; Pet. 22-23 & n.9. Attempting to belittle that inconsistency, respondents insist that the Second Circuit's decision is merely jurisdictional and does not resolve respondents' claims under Section 525. Br. in Opp. 11. Section 525 of the Bankruptcy Code, however, reaches only those debts that are "dischargeable *in the case under this title*," *i.e.*, debts dischargeable *in bankruptcy*. 11 U.S.C. 525(a) (emphasis added). By holding in this very controversy that bankruptcy and district courts cannot modify or discharge the full and timely payment condition of respondents' licenses, the Second Circuit's decision logically foreclosed application of Section 525 to this case. Indeed, while acknowledging the Second Circuit's ruling that "the bankruptcy court had no authority to modify" the FCC's timely payment condition, the D.C. Circuit suggested that "a court of competent jurisdiction (such as this one)" could do so. Pet. App. 42a. The D.C. Circuit's purported authority to discharge the payment obligation, however, does not exist—the authority to discharge debts is vested exclusively in the district and

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options, instead attempting to keep *all* of their licenses for one-quarter of the bid price. Pet. 7-8, 16.

bankruptcy courts overseeing reorganization proceedings. 28 U.S.C. 1334(a); 11 U.S.C. 1141(d)(1); Pet. 23. In any event, any purported nonbankruptcy power to discharge obligations would not satisfy the terms of Section 525, which requires the obligation to be dischargeable in the case under the Bankruptcy Code. See Pet. 23-24.

The D.C. Circuit's and the Second Circuit's opinions also conflict at a more fundamental level. The D.C. Circuit treated the FCC as an ordinary creditor. The FCC's decision to obtain liens on the licenses as a supplement to the FCC's regulatory authority, in the D.C. Circuit's view, created "standard debt obligations as part of its licensing scheme" and gave it "a creditor relationship with winning bidders." Pet. App. 2a, 40a-41a, 50a. See also Br. in Opp. 20-21. In contrast, the Second Circuit made it clear that any attempt to "turn the FCC into a mere creditor" is "fundamentally mistaken"—even if, "[i]n granting licenses by auction, the FCC acts as creditor and regulator both." Pet. App. 234a-235a, 244a. The agency's "regulatory function is not ended by the bankruptcy of a licensee or license claimant," the Second Circuit held, "and as the *function persists it must perforce be carried out*." *Ibid.* (emphasis added).

3. Respondents argue that the decision below rests on an alternative ground—that the Bankruptcy Code's automatic stay, 11 U.S.C. 362, precluded the FCC from canceling the licenses, because cancellation was tantamount to the enforcement of a lien. The court of appeals, they contend, held that there is no "regulatory exception" to the automatic stay's prohibition on lien enforcement, 11 U.S.C. 362(a)(4)-(5). See Br. in Opp. 19-20. Contrary to respondents' claim, the opinion below nowhere suggests that its discussion of lien enforcement *independently* supports its judgment. To the contrary, the D.C. Circuit made it clear that the judgment rests solely on its construction of Section 525: "In view of our conclusion that the Commission violated section 525 of the Bankruptcy Code in canceling NextWave's licenses," the court of appeals stated, "*we need not consider NextWave's remaining Bankruptcy Code arguments*." Pet. App. 51a

(emphasis added). The D.C. Circuit did discuss (*id.* at 40a-41a) the application of the automatic stay to lien enforcement efforts, but it did so in *support* of its determination that cancellation of respondents' licenses violated Section 525—specifically, in rejecting the argument that Section 525 should be construed consistent with the Code's structure of preventing bankruptcy law from intruding on regulatory action. See Pet. App. 40a-41a; Pet. 9. Because the D.C. Circuit relied on that reasoning to support its reading of Section 525, it is encompassed within the question presented, Pet. i, as the petition itself makes clear, Pet. 28 n.10.

The D.C. Circuit's reasoning on this point, moreover, defies common sense—and underscores the inconsistency between its decision and the Second Circuit's. Even if the automatic stay prevented the FCC from collecting payment based on the *liens* on respondents' licenses, the full and timely payment requirement nonetheless would retain its character as a regulatory license condition.[5] And because that condition is regulatory in nature, 11 U.S.C. 362(b) excepts it from the automatic stay. Indeed, the Second Circuit expressly so held. Pet. App. 125a (because the "FCC is a governmental unit that is seeking 'to enforce' its 'regulatory power,'" enforcement of payment condition is exempt from automatic stay); see also *id.* at 33a-35a. The decision below never explains why the Commission's decision to create a lien interest in the licenses *in addition to* its regulatory powers somehow deprived the FCC of authority to exercise its regulatory powers. The decision below never explains how that conclusion can be reconciled with the documents that created the liens, which specify that the liens supplement, but do not displace, the FCC's regulatory authority. See Pet. App. 403a-404a; Pet. 29 n.10. And the decision below never reconciles its analysis with the Second

[5] It is far from clear that the automatic stay applies at all. See Pet. 28 n.10. The Second Circuit, moreover, specifically rejected the claim that the lien-enforcement provisions of the automatic stay prevent the FCC from enforcing regulatory payment requirements. Pet. App. 125a & n.7.

Circuit's conclusion that cancellation of respondents' licenses is regulatory action exempt from the automatic stay, even if the FCC can be characterized as having both regulatory and pecuniary interests. See Pet. App. 125a-126a; p. 7, *supra*.[6]

4. Finally, respondents attempt, but fail, to rehabilitate the D.C. Circuit's analysis on the merits. Section 525, by its terms, prohibits governmental agencies from revoking licenses only if they do so *solely because* a debtor has failed to pay a *debt that is dischargeable in bankruptcy*. 11 U.S.C. 525(a). Respondents' Section 525 argument fails on both counts. Respondents' licenses canceled because respondents failed to comply with a regulatory requirement that was imposed as a condition of licensure—a condition that, as the Second Circuit recognized, could not be altered or discharged in bankruptcy. See pp. 6-7, *supra*; Pet. 22-23 & n.9. Likewise, the FCC did not revoke respondents' licenses "solely because" of the nonpayment of a "debt." The government was not concerned only, or even primarily, with the financial consequences of nonpayment. Instead, cancellation followed default as a regulatory matter because respondents' failure to stand behind their winning bids refuted their claims to be the best user of the spectrum.[7]

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[6] Respondents also contend that the judgment below is "supported by additional alternative grounds *not* resolved by the D.C. Circuit." Br. in Opp. 21-22 (emphasis added). The alternative ground respondents present —that the FCC violated due process by providing insufficient notice that their licenses would cancel on nonpayment—is without merit. The licenses and the Commission's rules unambiguously provided for license termination for failure to meet regulatory payment obligations. See Pet. 4, 5-6; 47 C.F.R. 1.2110(e)(4) (1997); Pet. App. 388a, 393a, 413a. In any event, any such constitutional claim may be addressed by the court of appeals after any remand by this Court. Nor does this Court's denial of certiorari in *In re GWI PCS 1, Inc.*, 230 F.3d 788 (5th Cir. 2000), cert. denied, 121 S. Ct. 2623 (2001), weigh against review. Although *GWI* was related to this case because both involved the intersection of bankruptcy and communications law, the *GWI* petition concerned the bankruptcy law doctrine of equitable mootness, see 230 F.3d at 799-805, a doctrine upon which this Court has never opined, and which is not involved in this case.

[7] Respondents mischaracterize the FCC's position when they assert that, under it, Section 525 would "be deemed inapplicable whenever an

By holding that the Bankruptcy Code nonetheless bars the FCC from withdrawing licenses for breach of the regulatory payment requirement, the D.C. Circuit unnecessarily converted Section 525(a) into an impediment to the market-based spectrum allocation mechanism established in Section 309(j). See Pet. 21-22. By preventing the FCC from enforcing that requirement, the court contravened Section 309(j)'s express direction that "[n]othing * * * in the use of competitive bidding"—including the fact that bidding results in payment obligations—"shall diminish the authority of the [FCC] * * * to regulate or reclaim spectrum licenses." 47 U.S.C. 309(j)(6)(C). See Pet. 26. And by treating the FCC as a mere creditor and the regulatory payment obligation as a dischargeable debt, the D.C. Circuit adopted a view of Section 309(j), the FCC's role, and the Bankruptcy Code that is irreconcilable with the decisions of the Second Circuit in this very case. Accordingly, this Court's review is warranted.

Respectfully submitted.

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agency chooses to promulgate a regulation making payment of debts a regulatory condition of licensure." Br. in Opp. 27. It is not enough that a payment requirement purport to be regulatory. The requirement in fact must serve a regulatory purpose. In this case, both the Second Circuit and the D.C. Circuit agreed that the FCC's full and timely payment requirement serves a regulatory rather than financial purpose. Pet. App. 24a, 125a-126a, 228a-230a. Respondents err in asserting (Br. in Opp. 26) that courts "uniformly hold that 525(a) is applicable" where the payment requirement "serves regulatory interests." The cases they cite involved efforts to use licensure as a means of collecting debts for financial purposes. They did not involve payment requirements that serve regulatory purposes, such as identifying the applicant that will best use an exclusive license in the public interest.

[*] The Solicitor General is disqualified in this case.