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NextWave: The Double Edged Sword

Paige E. Barr*

I. Introduction

The role of regulatory agencies once a debtor declares bankruptcy was the center of debate for many years. It was unclear what powers, in regard to licenses issued to regulatory companies, the regulatory agency held after the company filed bankruptcy. On a number of occasions, courts rejected arguments by government agencies that they should be exempted from various provisions of the Bankruptcy Code ("Code") that contain no explicit government exceptions. In 2003 the Supreme Court considered the issue and refused to except a regulatory agency from a section of the Code that did not contain a governmental exception. Specifically the Court prohibited the Federal Communications Commission ("FCC") from revoking commercial spectrum licenses from parties that had defaulted on their required installment payments.

The implications of the NextWave decision are two-sided. First as to the benefits of NextWave, the decision brought certainty to governmental agencies when dealing with bankrupt companies. Secondly, the decision promotes the function and theories of the Bankruptcy Code. Third, it has enabled companies, such as NextWave, to reorganize, whereas before they were left without any assets to stimulate reorganization. Finally, the NextWave decision clearly delineates that governmental agencies must comply with all laws, not just those that they oversee.

However, the decision has also left some unanswered questions and difficult implications. The aftermath of the NextWave decision has completely invalidated the purpose of the Federal Communications Act of 1934, it has subordinated important public policies, and has failed to provide a clear understanding of the bankruptcy courts' jurisdiction when dealing with governmental agencies.

II. BACKGROUND

In order to understand the concepts behind the Court's decision as well as its implications, a basic understanding of various sections of the Bankruptcy Code as well as the Federal Communications Act is needed.

A. Bankruptcy Court Jurisdiction over Property of the Estate

When a debtor files bankruptcy § 362 of the Code provides an automatic stay of all creditor efforts to obtain property of the estate. The automatic stay prevents creditors from attempting to collect from the debtor. It becomes effective immediately upon a debtor's filing and does not require judicial action. The debtor's benefit from the automatic stay is that the stay relieves the debtor of creditor harassment and allows assessment of the debtor's financial situation without interference from creditors. Failure to provide the debtor this period of reprieve would drastically limit the debtor's chance for reorganization. Creditors also benefit from the automatic stay since it guarantees that the assets of the estate will be preserved for equal treatment in the bankruptcy proceedings.

While § 362(a) provides for the automatic stay, § 362(b) provides exceptions to the automatic stay. Section 362(b)(4) states that the filing of a bankruptcy petition does not operate as a stay to a governmental unit seeking to enforce its police or regulatory powers against a debtor. Section 362(b)(4)'s legislative history suggests that while the exception should allow the governmental body to pursue legitimate police power and regulatory goals, it should not apply so as to

2. Id.
3. Id. While the automatic stay takes effect immediately, the bankruptcy court's authority to invoke the stay depends on a jurisdictional grant of authority that permits its enforcement. The Bankruptcy Court is granted authority for invoking the stay from § 1334(e) of the Code and Title 11. Section 1334(e) grants the district court exclusive jurisdiction over all property of the debtor, wherever it is located. 11 U.S.C. § 1334(e) (2004). The power granted in § 1334 may be exercised by the bankruptcy court after a district judge assigns the case to a bankruptcy judge under Title 11. Thus, the court may conduct a uniform proceeding in a single forum.
5. Id. at 949.
6. Id. at 947-48.
except agency action whose aim is to "protect a pecuniary interest in property of the debtor or property of the estate." 9

In the years preceding the NextWave decision, courts primarily used two tests to determine if a regulatory agency is excepted from the automatic stay: the "pecuniary purpose" test and the "public policy" test. 10 Under the "pecuniary purpose" test, a governmental unit was not excepted from the stay if it primarily sought to protect a pecuniary interest. 11 The test attempted to distinguish between an effort to protect the government's pecuniary interest or a public policy effort. 12 Naturally, the "public policy" test determined whether the government sought to effectuate public policy or to adjudicate private rights. 13 Actions to advance private rights by the government were not excepted from the stay. 14

B. Bankruptcy Code's Prohibition on Discrimination of Those in Bankruptcy

Section 525(a) of the Bankruptcy Code prevents any governmental unit from "revoking, suspending, denying or refusing to renew, or discriminating in any way with respect to, a government license, permit, employment, or other similar grant' to a debtor or former debtor or its affiliate 'solely because' the debtor is or was in bankruptcy, was insolvent before it was adjudged a bankruptcy, or did not pay a debt dischargeable in the bankruptcy case." 15

Section 525(a) was a source of dispute among courts well before the NextWave decision. Most of the litigation centered on the interpretation of the statutory language "other similar grant" 16 and the clause

10. See Pardo, supra note 4, at 949 (citing Universal Life Church, Inc. v. United States (In re Universal Life Church, Inc.), 128 F.3d 1294 (9th Cir. 1997) (finding that, under either test, IRS letter revoking tax exempt status of Chapter 11 debtor-religious organization fell within police/regulatory exception); NLRB v. Cont'l Hagen Corp., 932 F.2d 828, 833 (9th Cir. 1991) (noting that "NLRB actions have been exempted from the automatic stay under both analyses"), Eddleman v. U.S. Dep't of Labor, 923 F.2d 782, 791 (10th Cir. 1991) (holding that Department of Labor's enforcement proceedings are exempt from stay under either test), overruled in part on other grounds, Temex Engery, Inc. v. Underwood, Wilson, Berry, Stein & Johnson, 968 F.2d 1003 (10th Cir. 1992) (involving finality of bankruptcy orders); NLRB v. Edward Cooper Painting, Inc., 804 F.2d 934, 942 (6th Cir. 1986) (holding NLRB unfair labor practice proceeding to be excepted from automatic stay under either test)).
11. Eddleman, 923 F.2d at 791.
12. Id.
13. Id.
14. Id.
"not solely because." Many courts refused to apply § 525(a) when the government's action was found to have occurred "not solely because" the debtor was bankrupt. Actions considered "not solely because" include denying or revoking a racing license when it was found that the debtor lacked financial integrity and future financial resources, and that the local market was saturated as well as revocation of debtor's license when the license had previously been suspended three times for failing to maintain insurance, the debtor held racing related debts, and was in bankruptcy.

In *NextWave* the Court had to decide a conflict between federal statutory provisions as well. The Court was called on to determine if § 525(a) conflicted with the Federal Communications Act, and if so, which statutory provision controlled.

C. Federal Communications Act

The Federal Communications Act of 1934 (hereinafter "FCA") established the FCC. The FCA was designed to control all radio transmission channels through the use of licenses granted by federal authority. The FCC was granted the power to issue radio licenses upon its determination that doing so will serve the "public interest,

§ 525(a) to (1) prevent a state mortgage fund from denying a mortgage to a former debtor, . . . (2) denying Florida taxing authorities' attempt to prevent a debtor from obtaining a certification showing that all state and county taxes were paid, where the taxes were dischargeable in the debtor's bankruptcy proceeding, and (3) preventing the government from revoking a real estate license for which payment had been made from a government real estate recovery fund. However, other courts have refused to apply § 525(a) in cases involving state-funded mortgage assistance payments, the eviction of a public housing tenant where pre-petition rent payments were discharged in bankruptcy, and the application of a driver's license restoration fee.

19. *FCC v. NextWave*, 537 U.S. 293 (2003). Around the same time as the *NextWave* decision, the Second Circuit also issued a decision strengthening the protections to debtors under § 525(a). *In re Stoltz*, 315 F.3d 80, 95 (2d Cir. 2002). The *Stoltz* Court applied § 525(a) to bar the eviction of a debtor from public housing even though she failed to pay pre-petition rent and the obligation to pay such rent had been discharged in her bankruptcy case. *Id.* at 89. The court held that a public housing lease was an "other similar grant" under § 525(a). *Id.* The Housing Authority argued that § 365, the Code's executory contract provision, required the debtor to cure the rent default as a condition of assuming the housing lease. *Id.* Thus, § 365 presented a potential conflict with § 525(a)'s anti-discrimination mandate, which the court presumed prevented the eviction of a debtor for failure to pay pre-petition rent. The Second Circuit held that § 525 was more specific than § 365 because it applied only to governmental units and government licenses and permits. *Id.* at 93. The court stated that it is "a basic principle of statutory construction that a specific statute . . . controls over a general provision." *Id.* (citing *HCSC-Laundry v. United States*, 450 U.S. 1, 6 (1981)).
21. *Id.* § 309.
22. *Id.* § 301.
convenience, and necessity."23 Over the years Congress has amended the FCA to authorize the FCC to award licenses in different manners. Traditionally, comparative hearings were held to consider the qualifications of competing applicants.24 In 1982, the FCA was amended to authorize use of a lottery system in awarding licenses.25

Most recently, in 1993 the FCA was amended to authorize use of competitive bidding, i.e., auctions.26 The auction procedure was chosen to further develop and speed the development of new technologies and services to benefit the public;27 assist in the recovery of the public spectrum;28 and promote efficient and intensive use of the spectrum.29 Congress also hoped to eliminate administrative or judicial delays.30 In order to promote economic opportunity and competition, and to eliminate the fear of an increase in concentration among the telecommunications industries, Congress instructed the FCC to issue licenses to a wide variety of applicants.31 In order to accomplish this objective, the FCC was given, *inter alia*, the flexibility to design alternate payment schedules for smaller companies bidding on the spectrum.32

The FCC decided to designate two of the six auction blocks of spectrum to broadband "Personal Communications Services" ("PCS"), i.e., the C and F blocks.33 The licenses were to be awarded through simultaneous, multiple round auctions.34 The C and F blocks were limited to only small businesses and other designated entities.35 Fur-

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23. *Id.* § 309(a).

- a carefully designed system to obtain competitive bids from competing qualified applicants [for electromagnetic spectrum licenses] can speed delivery of services, promote efficient and intensive use of the electromagnetic spectrum, prevent unjust enrichment, and produce revenues to compensate the public for the use of public airwaves.

28. *Id.* § 309(j)(3)(C).
29. *Id.* § 309(j)(3)(D).
30. *Id.* § 309(j)(3)(A).
31. *Id.* § 309(j)(3)(B).
34. *In re* Implementation of Section 309(j) of the Communications Act – Competitive Bidding, 9 FCC Rcd. 2348, ¶¶ 54, 68 (1994).
thermore, small businesses bidders were permitted to make installment payments.\textsuperscript{36} Under the grant of installment payments, C-block auction applicants were allowed to pay ten percent of their winning bid in cash by the time of the license grant,\textsuperscript{37} with the remainder to be paid over the ten-year term of the license.\textsuperscript{38} The FCC's auction rules specified that for applicants electing to pay in installments, any license granted "shall be conditioned upon the full and timely performance of the licensee’s payment obligations under the installment plan,"\textsuperscript{39} and the failure to make timely payments would automatically render the license cancelled.\textsuperscript{40}

D. Licensing Cases Before NextWave

In 2000 a Kansas district court, in \textit{United States v. Kansas Personal Communications Services, Ltd}, held that the FCC did not violate 11 U.S.C. § 362 by canceling licenses.\textsuperscript{41} Because the FCC regulations dictated that the licenses are automatically canceled upon default, the court found that the FCC did not act in violation of the automatic stay provisions.\textsuperscript{42} The court also found that the "police and regulatory exception" to the automatic stay was applicable to the cancellation of radio spectrum.\textsuperscript{43}

However, in \textit{GWI PCS 1}, the Fifth Circuit allowed the debtor's obligations to pay the FCC for electromagnetic licenses to be avoided.\textsuperscript{44} The debtor's payment obligations were found avoidable as constructive fraudulent transfers under § 548 of the Code and thus, the debtors were allowed to retain their FCC licenses as property of the estate.

E. NextWave's Participation in the Spectrum Auctions

NextWave Personal Communications, Inc., and NextWave Power Partners, Inc. (collectively referred to as NextWave), participated respectively in the FCC's "C-Block" and "F-Block" auctions.\textsuperscript{45} NextWave was a start-up company organized to take advantage of the opportunities provided by § 309(j) in the PCS industry.\textsuperscript{46}

\textsuperscript{36} Id. § 24.711.
\textsuperscript{37} Id.
\textsuperscript{38} Id. § 24.711(b).
\textsuperscript{39} Id. § 1.2110(g)(4).
\textsuperscript{40} 47 C.F.R. § 1.2110(g)(4)(iv).
\textsuperscript{42} Id.
\textsuperscript{43} Id.
\textsuperscript{44} \textit{In re GWI PCS 1 Inc}, 230 F.3d 788 (5th Cir. 2000), \textit{cert. denied}, 533 U.S. 964 (2001).
At the auctions, NextWave was the highest bidder for 63 C-Block licenses, totaling $4.74 billion, and 27 F-Block licenses totaling approximately $123 million. Following the C-Block auctions, NextWave submitted applications for those licenses upon which it was the winning bidder for review and approval by the FCC. Ninety percent of the highest bidders at the auction for C-Block licenses were granted their licenses on September 17, 1996. However, NextWave was not one of those parties. NextWave was required to wait longer than the other C-Block licensees because its ownership structure, specifically its allegedly impermissibly high percentage of foreign ownership was challenged.

The auction of D, E, and F Blocks began in August 1996 and lasted until January 1997. These blocks covered geographical areas across the country, including areas covered by the 63 C-Block licenses for which NextWave was awaiting approval. The winning bids on the D, E, and F block auctions were a fraction of the winning bids in the C-Block auction.

On January 3, 1997, NextWave was conditionally granted its licenses after it submitted a plan to bring its capital structure into compliance with FCC regulations. Finally, the FCC granted NextWave its licenses conditional upon NextWave issuing a series of promissory notes for the balance of its payments on February 14, 1997. Then, on February 19, 1997, in accordance with the FCC regulations, NextWave made a down payment on the purchase price, signed promissory notes for the balance, and executed security agreements that the FCC perfected by filing under the Uniform Commercial Code. The security agreements granted the FCC:

- a first 'lien on and continuing security interest in all of the Debtor's rights and interest in [each] License.' In addition, the licenses recited that they were 'conditioned upon the full and timely payment of all monies due pursuant to . . . the terms of the Commission's installment plan as set forth in the Note and Security Agreement

49. Id.
50. Id.
53. Id. at 266-67.
54. Id. at 267.
56. Id.
executed by the licensee,’ and that ‘failure to comply with this condition will result in the automatic cancellation of this authorization.’

Almost all of the C-Block licenses experienced great difficulty in obtaining the necessary financing as a consequence to the gross disparity in the value of the C-Block licenses to the other blocks. In early 1997 many of the C-Block licensees requested alternative financing arrangements due to their difficulty in obtaining financing and the inability to keep up with the installment payments plan. The FCC was responsive to these requests and suspended the C-Block installment payments indefinitely.

The FCC then initiated an elaborate administrative process for restructuring the C-Block license payments. In response to its consideration of the C-Block installment payments, the FCC issued a Restructuring Order on October 16, 1997. The Restructuring Order provided four distinct, mutually exclusive alternatives for the struggling C-Block licensees. Then on March 24, 1998, in response to many motions for reconsideration, the FCC issued a Reconsideration Order. The Reconsideration Order was virtually the same as the Restructuring Order except that it provided the licensees more flexibility in making their choices under the Restructuring Order. The FCC set a deadline of June 8, 1998 for the C-Block licensees to select a method of repayment. However, NextWave was still dissatisfied with the options available under the Reconsideration Order and petitioned the FCC and the District of Columbia Circuit Court for an extension of the June 8 deadline. Both the FCC and the D.C. Circuit Court denied NextWave’s requests and on June 8, 1998, instead of choosing an option under the Reconsideration Order, NextWave filed for Chapter 11 bankruptcy. The drastic devaluation in the C-Block licenses, as reflected in the values of the subsequently bid D, E and F

59. Id.
62. Id. The FCC reviewed over 160 public comments regarding the issue and held a public forum.
63. Id.
64. Id.
65. Id.
66. Id.
68. Id.
69. Id.
block licenses, was the central factor in the NextWave bankruptcy filing.\textsuperscript{70}

Upon filing for bankruptcy NextWave suspended all payments to the FCC.\textsuperscript{71} It then initiated an adversary proceeding in the bankruptcy court alleging that the money it owed to the FCC for the C-Block licenses was a fraudulent conveyance, under § 544 of the Bankruptcy Code, because by the time the Commission actually conveyed the licenses, their value had declined from approximately $4.74 billion to less than $1 billion.\textsuperscript{72}

F. NextWave Lower Court Decisions

The bankruptcy court concluded that NextWave's exchange of $474 million in cash and $4.27 billion in promissory notes for the C-Block licenses was not an exchange of reasonably equivalent value, and therefore was a fraudulent conveyance.\textsuperscript{73} It determined that the fair market value of the licenses was approximately $1 billion and thus subsequently held that $3.7 billion of NextWave's bid obligation to the FCC could be avoided.\textsuperscript{74}

In making its determination the bankruptcy court rejected the FCC's argument that, because only the courts of appeals may review final orders of the FCC, the bankruptcy court lacked jurisdiction to hear the fraudulent conveyance claim.\textsuperscript{75} Although the bankruptcy court acknowledged that governance of the auction process for the spectrum falls within the FCC's regulatory authority, and that any appeal over an FCC order regarding that process would fall within the

\textsuperscript{72} Id. at 297-98.
\textsuperscript{73} NextWave Pers. Communications, Inc. v. FCC (In re NextWave Pers. Communications, Inc.), 235 B.R. 305 (Bankr. S.D.N.Y. 1999). Section 544(b) of the Code allows the avoidance of "any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under the applicable law." 11 U.S.C. § 544(b) (2004). "Applicable law" includes various state fraudulent conveyance statutes, many based on the Uniform Fraudulent Transfer Act. Sender v. Simon, 84 F.3d 1299, 1304 (10th Cir. 1996). "In analyzing fraudulent conveyance claims under the act, courts determine whether the debtor was engaged or about to engage in a transaction for which the remaining assets of the debtor were unreasonably small in relation to the size of the transaction. If so, and if the consideration provided by the debtor for the allegedly fraudulent transfer was not reasonably equivalent to what the debtor received in return on the effective date of the transfer, then the transfer is deemed constructively fraudulently and can be avoided." FCC v. NextWave Pers. Communications, Inc. (In re NextWave Pers. Communications, Inc.), 200 F.3d 43, 49 (2d Cir. 1999).
\textsuperscript{74} Id. at 297-98.
jurisdiction of the courts of appeals, it did not view the restructuring orders by the FCC as relating to its regulatory function.\textsuperscript{76} To do so would give the FCC the authority to define its own status as a creditor in relation to its licenses or its licensees' creditors, and, in the process, sidestep federal bankruptcy law.\textsuperscript{77} After finding that it had jurisdiction to consider the claim, the court found the FCC to be a creditor in this case, and that nothing in "§ 309(j) or elsewhere in the FCA or in the Bankruptcy Code states that the FCC is exempt from any of the provisions of the Code which affect is as a creditor."\textsuperscript{78} Thus, the FCC was subject to NextWave's fraudulent conveyance claim and the FCA does not conflict with or preempt state fraudulent conveyance law.\textsuperscript{79}

The district court affirmed.\textsuperscript{80}

On appeal,\textsuperscript{81} the Second Circuit reversed the district court's affirmance of the bankruptcy court's orders.\textsuperscript{82} The court reasoned that, be-

\textsuperscript{76} Id.
\textsuperscript{77} Id.
\textsuperscript{78} Id.

\textsuperscript{79} Id. NextWave also contended that FCC engaged in misconduct by acting in its regulatory capacity. NextWave alleged in its Amended Complaint that "[t]he FCC completely controlled all aspects of the C-Block auction process, including the rules, timing, and manner in which the C-Block licenses were issued to [NextWave]. The C-Block licenses constitute all or substantially all of the [NextWave's] assets. The FCC thus controlled [NextWave's] business and all of its assets." The bankruptcy court refused to consider the merits of this claim because it found it did not have subject matter jurisdiction to adjudicate the propriety of the FCC's regulatory conduct. Id. at 271. The claim was never appealed by NextWave.


cause courts of appeals, pursuant to 28 U.S.C. § 234283 and 47 U.S.C. § 402,84 have exclusive jurisdiction over claims challenging final orders of the FCC, the bankruptcy court lacked jurisdiction to determine whether the automatic stay applied to the FCC.85 Holding that the allocation of radio spectrum licenses lay within the FCC’s regulatory purview, the Second Circuit found that the bankruptcy court lacked jurisdiction over NextWave’s claim.86

Soon after the Second Circuit’s decision, the value of licenses rapidly began to rise.87 NextWave proposed a plan of reorganization that would give the FCC $4.3 billion, including interest and late fees.88 However, the FCC refused NextWave’s plan and offered the licenses for re-auction.89 The FCC believed that the licenses had been cancelled under the automatic cancellation provisions in the security agreement.90 The FCC re-auctioned the licenses and received approximately $16 billion for them.91

NextWave sought reconsideration by the FCC on the license cancellation. The FCC denied this request.92 NextWave challenged the sale of the licenses as a violation of the automatic stay.93 The bankruptcy court agreed and held the sales void.94 The bankruptcy court held that the conduct of the FCC, in declaring debtors in default of their obligation to make installment payments to the FCC, and in notifying debtors that licenses had been automatically cancelled, violated the automatic stay as an attempt by the FCC to exercise control over licenses constituting “property of the estate.95 Furthermore, the “automatic cancellation” of debtors’ licenses also violated the stay.96

83. 28 U.S.C. § 2342 (2004) (delineating the instances in which courts of appeal have exclusive jurisdiction to enjoin, set aside, suspend, or determine the validity of certain actions).
86. Id.
89. Id. at 138 (quoting FCC Public Notice DA00-49, Auction of C and F Block Broadband PCS Licenses, 15 F.C.C.R. 693, 693 (Jan. 12, 2000).
90. Id.
94. Id.
95. Id.
96. Id.
Sticking to its jurisdictional ruling, the Second Circuit again reversed. NextWave appealed the decision to the D.C. Circuit. There NextWave argued that the FCC had violated the automatic stay and the antidiscrimination provisions of the Code. The D.C. Circuit ruled in favor of NextWave. It held that the FCC had violated the antidiscrimination provision of § 525(a), which states that "a governmental unit may not deny, revoke, suspend, or refuse to renew a license . . . solely because such bankrupt or debtor . . . has not paid a debt that is dischargeable . . . under the Bankruptcy Act." The court furthermore rejected the FCC's argument that its automatic cancellation of NextWave's licenses constituted a regulatory action exempt from § 525, since none of the enumerated exceptions in the Code authorized the FCC's actions. In conclusion, the court ordered reinstatement of NextWave's licenses and reiterated the point that even though the government is a creditor, a company's right to a fresh start should not be impaired.

G. Supreme Court Decision

In its appeal to the Supreme Court, the FCC argued that 1) it did not revoke NextWave's licenses "solely because" of nonpayment, 2) NextWave's obligations were not debts that were dischargeable under the Code, and 3) that the circuit court's interpretation of § 525 brings it in conflict with the FCA. The Supreme Court affirmed the D.C. Court of Appeals. The Court held that § 525 prohibits the FCC from revoking licenses held by a debtor upon the debtor's failure to make timely payments to the FCC for the purchase of licenses. The Court first rejected the FCC's argument that it did not revoke NextWave's licenses "solely because" of nonpayment. The Court held that the fact that the FCC had a valid regulatory motive for its action

97. In re FCC, 217 F.3d 125, 141 (2d Cir. 2000).
100. Id. § 525(a).
102. Id. at 152.
103. Id. The court also held that the "Code expressly contemplates that bankrupts will sometimes avoid the consequences of late or non-payment they might have faced had they not filed for bankruptcy." Id. Furthermore, when the FCC decided to allow the Restructuring Order, it should have expected that its financing activities would be treated no differently than those of any other creditor. Id.
104. Id. at 156.
106. Id. at 308.
107. Id.
108. Id. at 301.
was irrelevant, since "[§] 525 means nothing more or nothing less than that the failure to pay a dischargeable debt must alone be the proximate cause of the cancellation, whatever the agency's ultimate motive may be."109

The Court went on to also reject the FCC's argument that regulatory conditions, like full and timely payments, are not properly classified as "debts" under § 525(a).110 Under the Code "debt" means "liability on a claim,"111 and "claim" includes any "right to payment,"112 and "right to payment" means an enforceable obligation, regardless of the Government's objective in imposing the obligation.113

The FCC's argument that NextWave's obligations are not dischargeable under § 525 because it is beyond the bankruptcy courts' jurisdictional authority to alter or modify regulatory obligations also failed.114 The Court reasoned that dischargeability is not tied to the existence of such authority.115 The Code only excepts the debts described in § 523 from discharge.116 Therefore, the FCC's argument that the D.C. Circuit had no power to modify or discharge a debt is irrelevant to whether that court can set aside agency action that violates § 525.117 All the D.C. Circuit did was set aside the agency action for a violation of § 525 when it prevented the FCC from canceling licenses because of the failure to pay debts dischargeable by bankruptcy courts.118

Lastly, the Court rebuked the FCC's contention that § 525 creates a conflict with the Communications Act.119 The Court held that what the FCC described as a conflict, rather just equates to a policy preference on behalf of the FCC for selling licenses on credit and canceling licenses rather than asserting security interests when there is a default.120 Such administrative preferences on behalf of the FCC cannot be the basis for denying NextWave its rights.121

109. Id.
110. Id. at 303.
112. Id. § 101(5)(A).
115. Id.
118. Id. at 303-04.
119. Id. at 304.
120. Id.
121. Id.
Justice Breyer wrote the sole dissenting opinion in NextWave. He questioned why "the government, and the government alone, [should] find it impossible to repossess a product, namely a license, when the buyer fails to make installment payments." He insisted that the antidiscrimination provisions of the Bankruptcy Code demonstrate that Congress intended only to prevent discrimination based on a company's bankrupt status. Furthermore, Congress did not intend for the Code to "deprive the American public of the full value of public assets that it owns." Justice Breyer expressed worry over companies that use Chapter 11 strategically; that is, they merely promise to pay for a public asset, go into bankruptcy, avoid the payment obligation, and keep the asset.

H. Reauthorization Bill 1264

Less than one year after the Supreme Court's ruling, the FCC attempted to circumvent the Court's ruling through the FCC Reauthorization Act. The intent of the Reauthorization Act was to prohibit the Code from 1) applying to debt obligations arising from auctions under the FCA and 2) staying payment obligations when a debtor to the United States has failed to make payments or if its license has been cancelled. Furthermore, it requests that the debtor shall have no interest in the proceeds from the auction of any license reclaimed by the FCC.

I. Settlement of the Spectrum Issue

On April 19, 2004, the government and NextWave reached an agreement over the licenses. Under the agreement, which was approved by the Department of Justice, NextWave will be able to keep its licenses in many of the largest and most lucrative markets, including Baltimore, Boston, Detroit, Los Angeles, New York, Philadelphia,

123. Id. at 312.
124. Id. at 313.
125. Id.
126. Id. at 315.
128. Id.
129. Id. Ironically, shortly after the NextWave decision the FCC issued a statement to "faithfully implement the Court's mandate." Rick B. Antonoff, High Court Rebukes FCC in NextWave, 22-May Am. Bankr. Inst. J. 1, 43 (2003).
and Washington. In turn NextWave will return to the FCC more than seventy-five percent of the licenses that have been unused for some many years. Those licenses will be reauctioned. The government will also receive $1.1 billion on top of the $500 million down payment NextWave already made. It could also get additional money if NextWave sells its remaining licenses at sufficiently high prices. Under the agreement NextWave will be able to erase its debts to the government and retain licenses in many large markets.

III. Analysis

The NextWave decision is a double edged sword. While it brings certainty to governmental agencies involved with bankruptcies, promotes the function of the Bankruptcy Code and its policies, allows small financially challenged companies to reorganize it also has disfavored ramifications. The purpose of the FCA is essentially invalidated by the NextWave decision through the use of strategic Chapter 11 tools; important public policy issues are subordinated; and there is a lack of certainty as to the bankruptcy court’s jurisdiction when dealing with governmental agencies. However, despite these ramifications, there are still some benefits for the government as a result of the NextWave decision. First, the uncertainty in jurisdictional issues of the bankruptcy court may very well serve the best interests of the agencies; the issue of assuming or assigning executory contracts may also resolved, through indirect analysis; and finally there are still self-help tools that the FCC, or other agencies in its position, may use to leverage its position.

A. Benefits of the NextWave Decision

The NextWave decision has brought certainty to companies like NextWave as well as to the law governing governmental agencies. Before the Court’s ruling it was impossible for companies like NextWave to implement a reorganization plan since the success of the plan depended on the ability to use or resell its licenses. The NextWave decision also clarifies that governmental agencies are prohibited from

131. Id.
132. Id.
133. Id.
134. Id.
135. Id.
136. Labaton, supra note 130.
revoking licenses or taking other action against companies in bankruptcy under § 525 of the Code.\textsuperscript{138} Furthermore, it is now clear that governmental agencies must comply with all laws, not just the legislation that they are charged with enforcing, regardless of the existence of laws conflicting with such legislation.\textsuperscript{139}

B. Consequences of NextWave

Regardless of whether the Reauthorization Bill is passed or the fact that NextWave and the FCC eventually settled their difficulties, the NextWave decision has its consequences. First, commentators continue to argue that the decision invalidates the FCA's purpose by opening the door for strategic use of Chapter 11, which serves to frustrate the diversity goals of the FCA. Second, there are important public policy issues that are adversely affected by the decision. Third, the Court failed to address the jurisdiction of bankruptcy courts in matters concerning federal regulation. This leaves many of the previous bankruptcy cases good law and may serve to strengthen the government's position in bankruptcy court.

1. Invalidating the Communications Act of 1934's Purpose Through Strategic Use of Chapter 11

As Justice Breyer's dissent states, the Court's decision implicates greater strategic use of the Chapter 11 and allows initiatives that may thwart the purposes of the FCA.\textsuperscript{140} For example, a company could make the initial down payment on a license, declare bankruptcy, and then still hold the licenses, essentially having an effective call option on them.\textsuperscript{141} The call option can be exercised in two ways. First, the company could choose to use the license, and then would just need to raise the necessary financing to bring itself out of bankruptcy.\textsuperscript{142} Or the company could choose to only capture a potential asset appreciation value without developing the license; in this circumstance the company has the option of negotiating a reorganization or a settlement.\textsuperscript{143} Finally, if the company does not prefer either option, the company can let the option expire by allowing the court to distribute the license in the normal course of the bankruptcy proceedings.\textsuperscript{144}

\begin{itemize}
  \item \textsuperscript{138} Id.
  \item \textsuperscript{139} Id.
  \item \textsuperscript{141} Federal Statutes and Regulations, 117 Harv. L. Rev. 390, 395 (2003).
  \item \textsuperscript{142} Id. at 396.
  \item \textsuperscript{143} Id.
  \item \textsuperscript{144} Id.
\end{itemize}
Another strategic use of Chapter 11 that the NextWave decision promotes is to allow companies the opportunity to improve their creditworthiness by filing a Chapter 11 petition. Debt investors can now rely on the fact that the government cannot revoke a license for nonpayment as long as the company invokes Chapter 11; thus, companies may now have an easier time obtaining capital to develop new technologies.

Unfortunately, most of these strategic uses that became available after the NextWave decision, frustrate the diversity goals of the FCA, which intended to make the telecommunications sector available to small businesses. These strategic uses enable concentration of the participation in spectrum use, an issue the FCA explicitly wanted to correct.

However, in response to the option market created by NextWave, there are still some options available to limit the strategic use of Chapter 11. Creditors still have the ability under the Code to obtain relief from the automatic stay through the use of the good faith and lack of adequate protection defenses. Under these defenses a creditor can lift the automatic stay and reclaim assets from bankruptcy. Section 362(d)(1) of the Code provides for relief from the stay “for cause, including the lack of adequate protection of an interest in property.” Furthermore, the Code requires a “good faith” requirement for confirmation of a bankrupt’s plan of reorganization. Therefore, a creditor may seek to invoke either of these defenses when seeking relief from the automatic stay.

In effect, the FCC’s attempt to obtain diversity in license ownership resulted in further speculation for small businesses involved in the auctions. In January 1998, the FCC announced its decision to dis-

145. Id. at 397.
146. Id.
147. 37 C.F.R. § 1.2110(g)(4)(iv).
149. 11 U.S.C. § 362(d)(1). A creditor can petition the court for relief from a stay, making a claim that the value of the collateral may decline during a bankruptcy restructuring. Even if the court does not lift the stay, it may require that the debtor provide “adequate protection” against a future diminution in value through cash payments, additional liens, or other means. Id. §§ 361, 362(d)(1)-(2).
150. Federal Statutes and Regulations, supra note 141, at 398.
152. Id. § 1129(a)(3).
154. Id.
continue the use of installment payments.\textsuperscript{155} Now bidders are required to pay the Commission in full and up front, thus eliminating the possibility of the government becoming a creditor since no security interest will be taken.\textsuperscript{156} However, this move really just shifted the market to the private sector, now smaller businesses without sufficient funding will have to secure private financing.\textsuperscript{157}

In August 2000 the government curtailed use of the diversity policies.\textsuperscript{158} In a very blunt way, this ended strategic abuse of Chapter 11. The FCC opened two-thirds of its licenses in major markets to all bidders, regardless of the diversity criteria.\textsuperscript{159} Ironically, but not surprisingly, the end of the diversity requirements unveiled the true participants in the diversity requirement era, as the large telecoms. Although NextWave itself was considered a start up company, Qualcomm and Sony provided most of its initial financing.\textsuperscript{160} The reauction was also played through pawns of the big companies; AT&T and Cingular both backed two of the key "entrepreneurs" in the bidding.\textsuperscript{161} Thus, with the end of the diversity requirements not much has changed. Smaller entrants are now merely further excluded from the telecommunications industry.

2. Subordination of Policy Arguments

Essentially, companies are now able to retain valuable assets in bankruptcy, rather than worrying about their public policy value. The Court's decision that the "fresh start" policy takes precedence over public policy, consequently subordinated some very important policy considerations. Most importantly, the broadband spectrum licenses, a valuable public good, went unused at a critical time for the telecomm-

\textsuperscript{155} Competitive Bidding Proceedings, 63 Fed. Reg. 2315, 2319 (FCC Jan. 15, 1998). Although the FCC's decision to end installment payments occurred before the Supreme Court's NextWave decision, its motive for doing so was clearly to anticipate the result that NextWave enabled: a situation in which a company could buy licenses on installment, pay only a down payment, and then lock up the licenses in bankruptcy. See id. (noting that the cancellation of installment payments would be effective "until controlling precedent is established or legislation . . . is enacted [to ensure that the] provisions of the Bankruptcy Code 1) are not applicable to any FCC license for which a payment obligation is owed; 2) do not relieve any licensee from payment obligations; and 3) do not affect the Commission's authority to revoke, cancel, transfer or assign such licenses"). That the FCC never received these assurances means that the cancellation of installment plans is likely permanent.

\textsuperscript{156} Federal Statutes and Regulations, supra note 141, at 398.

\textsuperscript{157} Id. at 398-99.


\textsuperscript{159} Id.

\textsuperscript{160} Federal Statutes and Regulations, supra note 141, at 399.

\textsuperscript{161} Id.
munications industry. Furthermore, the rights of the companies who innocently purchased the licenses on their reauction were completely disregarded. Finally, the public was prevented from collecting billions of dollars in secured claims from a debtor unable to provide adequate protection.

Throughout the NextWave litigation broadband spectrum licenses, which are valuable public goods, went unused at a critical time for the telecommunications industry. When the spectrum was initially auctioned to NextWave the intent was to spur technological innovation and further use of the spectrum creating efficient technology development. Leaving the spectrum in an unused state for almost eight years was not in furtherance of these goals. Furthermore, the FCC's attempt to reauction the licenses exacerbated the already existing slump in the wireless industry.

After the FCC reauctioned the licenses, NextWave obtained a judicial stay on the sales pending judicial determination of the issue. However, at this time the FCC failed to cancel the reauction results, even though it had no spectrum to give the winners. Thus, since the licenses were never delivered to the reauction winning bidders, these "winning bidders" effectively acquired large liabilities with no offsetting assets. Thus, until the settlement between NextWave and the FCC in April 2004, these licenses were held up in the bankruptcy process and not effectively being used and the industry suffered as well from making a large investment in the reauction without receiving any benefit. During the time that the FCC refused to refund or cancel the reauction results, the FCC's policy effectively served to harm the wireless service providers and equipment manufacturers, as well as taxpayers by lowering future auction receipts to the U.S. Treasury. At a time that the industry was already suffering from heavy debt and slow growth, the effect of the reauction investment did not makes the skies any more promising for the telecommunications industry.

While settlement has occurred between NextWave and the FCC and the spectrum is finally being set up for future use, the harm to the

162. Id.
163. Id.
164. Id.
165. Federal Statutes and Regulations, supra note 141, at 399.
168. Sidak, supra note 166, at 616-17.
169. Id. at 617.
170. Id.
industry in the interim period cannot be overlooked. Lost market values, lost jobs, and lower credit ratings for telecom companies were just some of the effects of the reauction dilemma.\textsuperscript{171} However, while this was not a favorable period of time for the telecommunications industry, there is certainty in the future after the \textit{NextWave} decision. The FCC is now well aware that it may not revoke licenses in this manner and also now knows how to prevent the tie-up of valuable licenses in bankruptcy. This knowledge will likely prevent any parallel future scenario.

The resolution of \textit{NextWave} was of great import to the bankruptcy system because it layed down the terms for everyone who invests in a business that relies on a license obtained via a security agreement.\textsuperscript{172} As discussed above, some commentators argue that the \textit{NextWave} decision allows any company holding any type of regulatory license to use the license as an option in bankruptcy on the underlying asset and as a means to lock out competition or to secure private financing.\textsuperscript{173} Alternatively, other commentators believe that Congress made a good policy choice, leaving the financial decisions, in all their many manifestations, to the bankruptcy system. This permits companies that need a license to operate and compete on equal footing for credit and investment dollars.\textsuperscript{174} Investors can safely take a risk in regulated businesses without the fear that regulators will shut the business down as soon as the company misses a payment.\textsuperscript{175}

3. Remaining Strength of Agencies Following \textit{Nextwave}

\begin{enumerate}[a.]
\item Jurisdiction

The \textit{NextWave} litigation could strengthen the government's usual position in bankruptcy proceedings through jurisdictional questions as well as the use of executory contracts. Furthermore, the FCC has self-help remedies available to it as well.

The Supreme Court did not address the jurisdiction of the bankruptcy court to consider the legitimacy of agency action. By not ruling on this issue, the Court let stand governing law in the courts of appeal that most frequently address administrative law and bankruptcy is-

\begin{footnotes}
\item[171] See generally id. for a more detailed explanation of the economic losses in the period of time following the reauction.
\item[173] Federal Statutes and Regulations, supra note 141, at 397.
\item[174] Warren & Westbrook, supra note 172.
\item[175] Id.
\end{footnotes}
The bankruptcy court's jurisdiction over issues that require review of agency action is severely limited by the Court's failure to consider the issue. The impact of this decision remains to be seen, not only on the bankruptcy courts' power to consider administrative action under the APA or *Chevron*, but also to consider antitrust enforcement agencies' challenges to bankruptcy proceedings, an issue that has remained a source of dispute.

b. Executory Contracts

While the Court did not explicitly address the issue of executory contracts in its decision, the Court's literal interpretation of the Code may be construed as favoring one side of this debated issue. Lower courts have grappled with the issue of whether § 365(c)(1)(A) absolutely bars trustees and debtors-in-possession from assuming executory contracts where applicable law excuses the nondebtor from accepting performance from a party other than the debtor or debtor-in-possession.

The language of the section is framed in terms of whether the trustee is proposing to "assume or assign" such an executory contract. Government agencies that are contractors with companies that file for Chapter 11 relief are particularly interested in the issue because the Anti-Assignment Act bars the assignment of government contracts. The Third Circuit, in *In re West Electronics, Inc.*, held that the effect of § 365(c)(1)(A) was to bar the debtor from assuming (not just assigning) a government contract that it had been performing before it filed for bankruptcy relief.

Cases addressing this executory contracts issue, have used two tests to interpret that statute: a "hypothetical" test and an "actual" test. The tests consider 1) whether the trustee is proposing to assign a non-
assignable contract or only seeking to assume it; and 2) if the debtor is only proposing to assume the contract, whether the section nevertheless applies where nonapplicable law would bar any assignment. 184

Commentators have argued that NextWave's literal interpretation of the Code favors the hypothetical test. 185 Proponents of the hypothetical test are usually government agencies that contracted with parties that became debtors-in-possession. 186 The agencies want flexibility to decide whether to immediately terminate a debtor's contract with the government agency. 187 Actual test proponents argue that a debtor should be able to assume the same contract it was performing before it filed for bankruptcy relief. 188 The NextWave decision rejected such policy considerations and may make lower courts more likely to side with the hypothetical test. 189

4. FCC's Own Remedies
a. Secured Creditor Status

Although the Court failed to indicate the import of the parties' debtor-creditor relationship, it did recognize that the FCC had a perfected security interest in the licenses. 190 The FCC should at least then possess the rights of a secured creditor. 191 Under general bankruptcy rules, if NextWave proposes to cure and reinstate its payment obligation pursuant to §§ 1123(a)(5)(G) and 1124(2)(a), it will be required to pay its debt in full. 192 If NextWave instead proposed to impair the Commission's debt by altering the terms or conditions of the obligation, the FCC should be entitled to the full value of its allowed secured claim. 193

184. Compare Perlman v. Catapult Entm't, Inc. (In re Catapult Entm't, Inc.), 165 F.3d 747, 750 (9th Cir. 1999) (using the hypothetical test), with Institut Pasteur v. Cambridge Biotech Corp., 104 F.3d 489, 493 (1st Cir. 1997 (using the actual test).
185. Perlstein & Bamberger, supra note 176, at 19.
186. Id.
187. Id.
188. Id.
189. Id.
192. 11 U.S.C. § 1123(a)(5)(G) provides that a bankruptcy plan shall "provide adequate means for the plan's implementation," such as "curing or waiving of any default." 11 U.S.C. § 1123(a)(5)(G) (2004). Section 1124(1) provides that claims are impaired under a plan unless that plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest." Id. § 1124(1).
In general, if a creditor is oversecured, i.e., the value of the collateral securing the claim is greater than the amount of the prepetition claim, it is entitled to insist on payment in full, plus interest, fees and costs. An undersecured creditor, by contrast, may either choose to have its claim bifurcated into secured and unsecured portions, or it may elect instead to insist on payment—full in nominal dollars: payments whose present value must equal the present value of the collateral and whose total value must equal the amount of the overall claim. These options should have been available to the FCC as a secured creditor.

b. Advanced Criteria

Furthermore, agencies may develop criteria for license awards that considers options other than the ability to meet monetary obligations. Considering criteria such as performance, financial health, service capacity and other nonmonetary standards would provide the agency with a strong argument that denial of the license was not based “solely” on nonpayment of monetary obligations. The agency should also establish a standardized practice in which it administers these standards. The more standardized the practice, the less it will lend itself to be discriminatory. This solution also finds support in the legislative history of § 525, which states that the statute “does not prohibit consideration of other factors, such as future financial responsibility or ability, and does not prohibit imposition of requirements such as net capital rules, if applied nondiscriminatorily.”

IV. Conclusion

The NextWave decision left benefit as well as consequence. However, the consequence may now be avoided forever if certain steps are initiated to prevent future instances such as NextWave. The FCC is now aware that it should not assume the role of a creditor when distributing licenses, and if it does it will be subject to the same rules as all other parties. The FCC is also aware that it must take alternative steps to make sure that revocation of a license in not classified as “solely” because of inability to make payments. Certainty has been

195. See id. § 506(a).
197. Id. at 21.
198. Id.
199. Id.
200. Id.
layed out in this area for governmental agencies to follow, and while it was a long tough battle to learn this lesson, the lesson has been learned. Furthermore, the government may still have strength within the issue of bankruptcy court jurisdiction as well as within the executory contracts area.

Finally, the main lesson of this saga may have been that if Congress determines that governmental agencies deserve more protection, then it should act. However, if Congress believes that the FCC is entitled to protection not already afforded by the Bankruptcy Code, it should achieve its goal through a process that fits within the existing bankruptcy framework. If, in a specific case the FCC believes it must be permitted to exercise its regulatory power, its actions should be subject to review by the bankruptcy court in the same manner currently required of all other governmental bodies and any change with respect to the FCC in the bankruptcy process should occur through the appropriate forum.