wiley

ALERT

FCC to Consider Sweeping Changes to Media Ownership Rules

October 27, 2017

Federal Communications Commission (FCC or Commission) Chairman Ajit Pai is proposing some of the most dramatic changes to the Commission's media ownership rules in decades. At its November 16 Open Meeting, the agency will consider an Order on Reconsideration that would: (i) eliminate the 42-year-old newspaper/broadcast cross-ownership rule; (ii) eliminate the radio/television cross-ownership rule; (iii) loosen the existing rules governing the ownership of local television stations (including attribution of joint sales agreements); and (iv) initiate a proceeding to establish an incubator program to facilitate the entry of new and diverse voices in the broadcast industry. If adopted, the Order on Reconsideration will represent a substantial departure from the Commission's Second Report and Order in the 2010/2014 Quadrennial Ownership Review (2016 Media Ownership Order), which largely left the FCC's existing rules intact.

Below, we summarize the key points from this draft order that Chairman Pai has released in advance of the November Open Meeting.

Newspaper/Broadcast Cross-Ownership Rule

The draft order would repeal the longstanding newspaper/broadcast cross-ownership rule, which is generally considered to be the lowest hanging fruit for deregulation. Under the existing rule, an entity cannot have an attributable interest in both a newspaper and a television or radio station in the same geographic area. In its 2002 Quadrennial Ownership Review, the FCC concluded that the rule is not necessary to promote the goals of competition or localism. Although the United States Court of Appeals for the Third Circuit agreed with the agency's findings, it struck down the order on other

Authors

Eve Klindera Reed
Partner
202.719.7404
ereed@wiley.law

Joan Stewart
Partner
202.719.7438
jstewart@wiley.law

Ari Meltzer
Partner
202.719.7467
ameltzer@wiley.law

Kathleen E. Scott
Partner
202.719.7577
kscott@wiley.law

Practice Areas

Media

Telecom, Media & Technology

grounds. Most recently, in its review of the 2010 Media Ownership Review, the Third Circuit lamented that "the 1975 ban remains in effect to this day even though the FCC determined more than a decade ago that it is no longer in the public interest."[1]

Nevertheless, the 2016 Media Ownership Order only moderately loosened the newspaper/broadcast cross-ownership rule concluding that some newspaper/broadcast cross-ownership restrictions continued to be necessary to promote viewpoint diversity. The 2016 Media Ownership Order created a case-by-case waiver standard and adopted other, minor, changes.

The draft order proposes to eliminate the newspaper/broadcast cross-ownership rule in its entirety, concluding that not only does it not advance localism and competition goals, but that it is no longer necessary to promote viewpoint diversity. The draft order also recognizes the potential benefits of cross-ownership to facilitate investment and achieve efficiences that will improve local news gathering.

Radio/Television Cross-Ownership Rule

The draft order would also repeal the radio/television cross-ownership rule, some version of which has been in effect since 1970. Under the existing rule, which was adopted in 1999, an entity can own varying numbers of radio and television stations depending on the size of the market. Permissible ownership combinations range from up to two television stations (subject to the local television ownership rule) and one radio station in small markets, to up to two television stations (subject to the local television ownership rule) and up to six radio stations, or one television station and seven radio stations, in large markets. In the 2006 Quadrennial Review, the agency found that the 1999 version of the rule should be retained, a decision that the Third Circuit found to be "plausibly justified."[2] However, in two notices of proposed rulemaking that preceded the 2016 Media Ownership Order, the Commission tentatively concluded that the rule is no longer necessary to promote competition, localism, or viewpoint diversity. In particular, the FCC noted that media ownership studies provided little evidence that radio/television cross-ownership impacted viewpoint diversity and discussed the growth of alternative media outlets, such as Internet and cable, as sources of viewpoint diversity. The Commission also suggested that the rule might not be necessary because radio stations are not primary outlets that contribute to viewpoint diversity.

Notwithstanding these prior tentative conclusions, in the 2016 Media Ownership Order the FCC retained the radio/television cross-ownership rule with only minor modifications. The Commission determined that the rule remains necessary to promote viewpoint diversity even though it had previously suggested the opposite. The agency also found that the rule serves public interest goals separate and apart from the local radio and local television ownership rules (discussed below), which primarily promote competition.

The draft order proposes to grant NAB's petition for reconsideration regarding the radio/television cross-ownership rule and to eliminate the rule in its entirety, based on a conclusion that the rule is no longer necessary to promote viewpoint diversity. The draft order determines that the earlier conclusion that radio stations contribute to viewpoint diversity to a degree that justifies retention of the rule was in error, particularly given evidence that consumer reliance on radio stations for news had declined significantly and the

decreasing number of all-news commercial radio stations. In addition, it concludes that the decision to retain the rule fails to take into account the realities of the digital media marketplace and the existence and growing number of other local media outlets to which consumers have access. It also finds that the rule does little to promote viewpoint diversity because it already permits a significant degree of common ownership – up to eight outlets in larger markets – and that elimination of the rule will not adversely impact minority and female ownership.

Local Television Ownership Rule

The draft order would grant, in part, petitions for reconsideration filed by NAB and Nexstar regarding the local television ownership rule, and revise that rule in two significant respects. The existing local television ownership rule allows a company to own up to two television stations in a local market only if (i) the digital noise limited service contours (NLSCs) of the stations do not overlap, and (ii) at least one of the stations is not ranked among the top-four stations in the market (the "Top Four Prohibition") and at least eight independently owned television stations would remain in the market after consummation of a proposed transaction (the "Eight Voices Test"). The draft order would revise the local television ownership rule by eliminating the Eight Voices Test and adopting a hybrid approach to the Top Four Prohibition that would allow for case-by-case analysis.

The current rule was adopted in 1999 and, following denial of reconsideration, challenged in court. The D.C. Circuit remanded the rule to the FCC, finding that the Eight Voices Test was flawed because it failed to consider outlets other than television broadcast stations.[3] In subsequent quadrennial review decisions, the Commission decided to retain the rule and was affirmed by the Third Circuit. The 2016 Media Ownership Order again retained (with only a minor technical modification) the 1999 version of the local television ownership rule, based on a determination that the rule remained necessary to promote competition. In that order, the FCC concluded that it was appropriate to focus on promoting competition among broadcast stations – rather than a larger market that would include non-broadcast video alternatives – for purposes of evaluating the continued appropriateness of the local television ownership rule. While recognizing that the video marketplace has changed significantly since 1999 and, particularly, in very recent years, the draft order would preserve the focus on competition among local television stations rather than including non-broadcast sources given the "unique and important role" of broadcast television.

At the same time, the draft order emphasizes that the very importance of local television stations makes it important to avoid unnecessary restrictions on television broadcasters in view of the constantly expanding video programming options available to consumers. In an effort to help television broadcasters achieve economies of scale and improve their ability to serve their local markets, the draft order would adopt two "common sense modifications" to the local television ownership rule.

First, the draft order would eliminate the Eight Voices Test, finding it to be unsupported by the record or reasoned analysis. Noting that the Commission has spent years seeking comment on the local television ownership rule, the draft order finds that the Eight Voices Test represents, at bottom, an arbitrary line. In addition, the draft order determines that the Eight Voices Test is inconsistent with the realities of the current

television marketplace and prevents combinations that would likely produce significant public interest benefits. Further, the draft order notes that small and mid-sized markets – in which the Eight Voices Test effectively prohibits common ownership of television stations – are those in which the efficiencies of common ownership can often produce the greatest benefits.

Second, the draft order would retain the Top Four Prohibition but modify it to include a case-by-case analysis where strict application of the rule may not be appropriate based on the circumstances of a particular market or transaction. The draft order finds that the record generally supported the FCC's prior determination that top-four combinations are associated with potential harms. At the same time, it notes that these harms may not be present with respect to all such combinations, and finds that the Top Four Prohibition is over-inclusive and should be modified. As a result, the draft order proposes to allow applicants to request a case-by-case examination of proposed combinations that would otherwise violate the Top Four Prohibition. While declining to adopt a rigid set of criteria to guide its case-by-case analysis, the Commission suggests that the following types of information could be relevant:

- Ratings share data of the stations proposed to be commonly owned compared with other stations in the market;
- Revenue share data of the stations proposed to be combined compared with other stations in the market, including advertising (on-air and digital) and retransmission consent fees;
- Market characteristics, such as population, the number and types of broadcast television stations serving the market, and whether there are any strong competitors outside of the top-four rated stations;
- The likely effects on programming meeting the needs and interests of the community; and
- Any other circumstances impacting the market, particularly any disparities primarily impacting small and mid-sized markets.

Applicants would be encouraged to provide data over a substantial period (*e.g.*, three years) to strengthen their requests for relief from the Top Four Prohibition in a particular case.

In addition to proposing these changes, the draft order concludes that the modifications are not likely to harm minority and female ownership, and reaffirms the previous determination that it remains premature to analyze the impact of the broadcast incentive auction on the local television ownership rule.

Local Radio Ownership Rule

The draft order would deny a petition for reconsideration of the FCC's decision in the 2016 Media Ownership Order to retain the current methodology for determining compliance with the local radio ownership rule in markets that contain embedded markets (*i.e.*, smaller markets, as defined by Nielsen Audio Metro (Nielsen), that are included in a larger parent market).

In the 2016 Media Ownership Order, the Commission did not revise the local radio ownership rule, which determines the number of radio stations that may be commonly owned in a given market. The rule relies on Nielsen methodology to define what constitutes a given radio market. In certain cases, a smaller Nielsen

market may be embedded within the boundaries of a larger Nielsen market. When demonstrating compliance with the local radio ownership rule, the entity must satisfy the ownership limits for both the embedded market as well as the larger parent market.

A petition for reconsideration of the 2016 Media Ownership Order argued that the FCC should adopt a new methodology for analyzing embedded markets. The petition argued that the Commission should adopt a new two-pronged test for an entity that seeks to own stations licensed to home counties in different embedded markets within a single parent market. The FCC had considered and declined to adopt this proposal when it was made in the underlying proceeding.

In again denying petitioner's proposed rule change, the draft order finds that the Commission's decision in the 2016 Media Ownership Order was supported by a reasoned explanation. The draft order asserts that petitioner's concern is better addressed in a market-specific waiver request rather than a change to the FCC's overall methodology. Likewise, the draft order affirms that the Commission's longstanding decision to evaluate the Puerto Rico market using a contour overlap mythology does not undermine its embedded market decision. Rather, the draft order explains that the uniqueness of the Puerto Rico market, specifically its mountainous topography, makes a comparison between it and typically embedded markets inapposite.

Television JSA Attribution

The draft order would eliminate the television Joint Sales Agreement ("JSA") attribution rule. The draft order would, on reconsideration, conclude that the FCC erred in its decision to adopt the television JSA attribution rule because (i) the underlying record did not support a finding of attribution, and (ii) the Commission failed to properly consider the public interest benefits of these arrangements.

The attribution of television JSAs has a long and tortured history. The FCC first considered whether to make these agreements attributable in 1999 but concluded that the agreements did not convey a sufficient degree of influence or control to warrant attribution. In 2004, the agency sought further comment on this conclusion. Then in 2014, relying on the decade-old proceeding, the Commission reversed course and adopted the television JSA attribution rule. In that decision, the FCC found that JSAs had the potential to allow the brokering station to exert significant influence over the brokered station and, thus, that television JSAs should be attributable. Following its adoption, the television JSA attribution rule was challenged on appeal. In vacating the rule, the Third Circuit determined that the rule was adopted prematurely because the Commission had not yet decided whether the Local Television Ownership Rule remained necessary.[4] Subsequently, the FCC concluded that the local television ownership rule did continue to serve the public interest and re-adopted the television JSA attribution rule. NAB and Nexstar then petitioned for reconsideration of that decision. This draft order grants those petitions for reconsideration.

The draft order would eliminate the television JSA attribution rule finding that the Commission's attribution analysis was deficient and did not adequately consider the record. Likewise, the draft order determines that the record contained ample evidence of the public interest benefits of JSAs, which the FCC failed to recognize.

In conclusion, the draft order asserts that eliminating the television JSA attribution rule is appropriate even with its decision to otherwise relax the local television ownership rule. The draft order acknowledges that there may be less need for television JSAs going forward. However, the Commission desires to preserve the right of television broadcasters to enter into television JSAs given the significant public interest benefits that can result from these agreements.

Shared Services Agreements

The draft order would decline to reconsider either the definition of Shared Services Agreements (SSA) or the disclosure requirement adopted in the 2016 Media Ownership Order. Rather, the draft order concludes that the adoption of both a definition and a disclosure requirement was fully supported by the record in that proceeding.

Significantly, the draft order affirms that this decision is not a pretext for further regulation of SSAs. Indeed, the draft order notes that should a future FCC consider the regulatory status of these agreements, it first must (i) demonstrate a significant study and understanding of the impact of these agreements on station operations and (ii) consider the public interest benefits these agreements help facilitate.

Diversity/Incubator Program and Notice of Proposed Rulemaking

The draft order would adopt a Diversity/Incubator Program ("Incubator Program") to promote new entry and ownership diversity in the broadcast industry. The Incubator Program has been discussed and debated for decades; most recently, the Commission declined to adopt the program, and NAB sought reconsideration of the issue. With this draft order, the FCC agrees with NAB that the Incubator Program should be adopted. However, the draft order also proposes to adopt a Notice of Proposed Rulemaking ("NPRM") regarding how to structure and monitor the Incubator Program, in light of what the Commission considers to be outstanding concerns.

The NPRM sets forth the FCC's vision for the Incubator Program. It will help provide capital and support for new and diverse media entrants. Additionally, the Incubator Program would provide a benefit to an established media company for helping to facilitate station ownership for certain classes of owners. The draft order gives the example of an established company receiving a broadcast ownership rule waiver for providing a new owner with "management or technical assistance, loan guarantees, direct financial assistance through loans or equity investments, training, or business planning assistance."

Specifically, the NPRM seeks comment on the costs and benefits associated with the Incubator Program and related proposals, as well as numerous questions related to the following topics:

- ***How to define entities eligible for Incubator Program participation.*** The Commission has proposed several options, including, at NAB's suggestion, a new entrant standard similar to the one that is applicable in the broadcast auction context; a revenue-based eligibility standard; a standard based on the Small Business Administration's definition of a socially and economically disadvantaged business; and a standard that would look to various criteria to determine if an entity has overcome significant

disadvantage.

- ***How to define qualifying incubation activities.*** The FCC's proposed NPRM makes clear that an incubation activity needs to provide the incubated entity with support that (i) it would otherwise lack and (ii) is essential to its operation and ability to serve the community. This support could be financial – such as loans or loan guarantees – or operational – such as business planning assistance. The Commission also proposed the concept of donating stations to certain organizations to allow a new entrant to gain operational experience without first having to acquire a station. The FCC is also interested in technical questions, like whether to impose time minimums or maximums for some activities and whether incubated entities need to make certain certifications.
- ***What meaningful benefit to provide incubating stations.*** The suggested benefit to incubating stations is waiver of the local broadcast ownership rules; however, the Commission has also asked about allowing the incubating entity to obtain an otherwise prohibited non-controlling attributable interest in the incubated station.
- ***Who should the program apply to.*** The FCC has asked whether the Incubator Program should apply to radio only, or to both radio and television. Additionally, the Commission asks if it should begin as a limited trial or as a fully expanded program.
- ***How the Commission should review incubation proposals.*** The FCC contemplates that most of the proposals for incubation relationships will be accompanied with an application to assign or transfer control, subject to the normal review process. The draft NPRM asks whether this is a sufficient review, and what the Commission should consider in evaluating the proposal. The NPRM also asks whether the Incubation Program should be open to existing media owners facing financial or technical difficulties, and if so, how such a proposal would be reviewed.
- ***How to assess compliance.*** The FCC asks how it should monitor compliance with the terms of incubation, and suggests tools such as periodic reports and public file requirements, among other things. The Commission also asks what the repercussions of non-compliance should be.

The draft contemplates that the newly commissioned Advisory Committee on Diversity and Digital Empowerment will play a key role in creating the Incubator Program.

The draft order, if adopted, will implement Chairman Pai's long-stated commitment to modernize the media ownership rules to "bring them into the digital age."[5] Chairman Pai has been vocal in his criticism of the FCC's antiquated ownership rules, arguing repeatedly that they stifle broadcasters' ability to compete in today's media marketplace. It is widely believed that the Chairman has the required votes to adopt the draft order, which will make the most significant changes to the media ownership rules in recent memory.

[1] *Prometheus Radio Project v. FCC*, 824 F.3d 33 (3d Cir. 2016) (*Prometheus III*).

[2] *Prometheus Radio Project v. FCC*, 652 F.3d 431, 457 (3d Cir. 2011).

[3] *Sinclair Broadcast Group v. FCC*, 284 F.3d 148 (D.C. Cir. 2002).

[4] *Prometheus III*, 824 F.3d at 57-60.

[5] Ajit Pai, *An Energetic November*, FCC Blog (Oct. 26, 2017), *available at* https://www.fcc.gov/news-events/blog/2017/10/26/energetic-november.