

SECURITY INTERESTS IN THE AIRWAVES: THE VIABILITY OF LIENS ON FCC LICENSES

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I. INTRODUCTION

For decades, the Federal Communication Commission (FCC) has refused to allow lenders to take security interests in FCC licenses on public policy grounds.¹ While this seems like a minor issue, it has become a significant impediment for broadcasters seeking communications-related funding. Problems most commonly arise in the bankruptcy context, and the debate about whether a pre-petition lien on an FCC license creates an enforceable post-petition interest in bankruptcy is not a new one.² However, the current state of the market makes the issue ripe for reevaluation.

Today, taking a security interest in a broadcast entity is a risky endeavor, because the failure of the entity licensee or termination of the FCC license has a devastating effect on the value of the collateral for the

1. See David Isenberg & Michael Reisz, *Toward a Compromise on Collateralizing Loans to Broadcasters*, 45 FED. COMM. L.J. 541, 542-44 (1993).

2. The issue of whether a lender may take a security interest in an FCC license came to a head in 1992. See *In re Ridgely Commc'ns, Inc.*, 139 B.R. 374 (Bankr. D. Md. 1992); *New Bank of New England, N.A. v. Tak Commc'ns, Inc.* (*In re Tak Commc'ns, Inc.*), 138 B.R. 568 (W.D. Wis. 1992).

creditor. The United States Bankruptcy Court for the District of Colorado recently disturbed what was deemed settled law and took a step backwards in what has been a slow forward crawl for broadcasters seeking funding over the past few decades.³

This Note provides a summary of the rules for protecting a security interest under Article 9 of the Uniform Commercial Code (UCC) and the potential collisions with the FCC and bankruptcy law. It then examines the evolution of the law regarding security interests in FCC licenses and highlights two recent bankruptcy court decisions that reached contradictory conclusions on the issue. The confusion created by the conflicting regimes of the UCC, the FCC, and the Bankruptcy Code suggests that the FCC should resort to the rulemaking process in order to offer greater predictability to lenders and borrowers, which would in turn facilitate transactions.

II. THE BASICS

The risks associated with taking a security interest in a broadcast entity highlight tensions among the different policy considerations underlying the UCC, the FCC, and the Bankruptcy Code. To understand how the policies interact, it is helpful to understand each in isolation.

A. Article 9 of the UCC

The UCC's objective in Article 9 is "to provide a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and with greater certainty."⁴ Article 9 reduces transaction costs "primarily by relaxing legal requirements for creating liens."⁵ The ease with which security interests may be created encourages lending and promotes commercial activity.⁶

Article 9 governs "all consensual security interests in personal property and fixtures."⁷ Subsection 9-109(a)(1) extends the scope of Article 9 to include "a transaction, regardless of its form, that creates a security interest

3. *Spectrum Scan LLC v. Valley Bank & Trust Co. (In re Tracy Broad. Corp.)*, 438 B.R. 323 (Bankr. D. Colo. 2010), *aff'd*, 469 B.R. 55 (D. Colo. 2011), *rev'd*, 696 F.3d 1051 (10th Cir. 2012).

4. U.C.C. § 9-101 cmt. 4 (2002).

5. Alan Schwartz, *Security Interests and Bankruptcy Priorities: A Review of Current Theories*, 10 J. LEGAL STUD. 1, 5 (1981).

6. WILLIAM H. LAWRENCE, WILLIAM H. HENNING & R. WILSON FREYERMUTH, *UNDERSTANDING SECURED TRANSACTIONS* 3 (4th ed. 2007).

7. § 9-109 cmt. 2.

in personal property or fixtures by contract,” which permits general intangibles such as FCC licenses to be taken as collateral.⁸

A security interest is enforceable only when it attaches to the collateral.⁹ There are three requirements for attachment: there must be a security agreement granting the security interest, the secured party must give value, and the debtor must have rights or the power to transfer rights in the collateral.¹⁰ If the security interest is to include after-acquired property, that must be provided for in the agreement.¹¹ But, a security interest automatically attaches to proceeds regardless of whether they are included in the security agreement.¹² The UCC defines proceeds broadly,¹³ and “[i]n effect, virtually anything that replaces the economic value of collateral constitutes a proceed.”¹⁴ The limitation is that proceeds must be identifiable, as the security interest terminates once the connection to the collateral is broken.

A secured party enhances its position against third-party claims to the collateral by “perfecting” its security interest and thereby giving public notice.¹⁵ Security interests are effective against unsecured creditors outside bankruptcy, and allowed secured claims in bankruptcy must be fully satisfied.¹⁶ Although possession is the most effective mechanism of perfection, it is often impractical and even impossible with certain forms of collateral, such as general intangibles.¹⁷ The default method of perfection under Article 9 requires that a financing statement indicating the collateral be filed in the debtor’s name in the designated state filing office.¹⁸ Finally,

8. § 9-109(a)(1); 9-102(42) (“‘General intangible’ means any personal property, including things in action, other than accounts, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, or other minerals before extraction. The term includes payment intangibles and software.”)

9. LAWRENCE, HENNING & FREYERMUTH, *supra* note 6, at 70.

10. § 9-203.

11. *See* § 9-204. An after-acquired property clause is beneficial, as a secured creditor can look to more items as collateral to get his or her debt repaid if the debtor files for bankruptcy.

12. *See* § 9-315.

13. *See* § 9-102(a)(64).

14. LAWRENCE, HENNING & FREYERMUTH, *supra* note 6, at 89.

15. § 9-308 cmt. 2 (providing that perfection usually involves giving notice, but certain security interests are perfected on attachment without the giving of notice).

16. *See id.* § 9-301 cmt. 1 (2002) (defining a perfected security interest as “a security interest in personal property which cannot be defeated in insolvency proceedings or in general by creditors”). *See also* LAWRENCE, HENNING & FREYERMUTH, *supra* note 6, at 227–29.

17. *See* § 9-313(a) (“General intangibles” cannot be perfected by possession and must be perfected by filing.).

18. *See* §§ 9-501 to 9-504; *see also* § 9-310(a). Certain distinct categories of collateral are perfected by attachment or by the secured party taking possession of the collateral. *See, e.g.*, §§ 9-309, 9-315, 9-311(a), 9-313.

a secured party cannot enforce its security interest against the collateral until the point of default.¹⁹

The framework of Article 9 provides a general “step-back” provision that makes Article 9 inapplicable where “a statute, regulation, or treaty of the United States preempts this article.”²⁰ The official comments note that this provision “recognizes explicitly that this Article defers to federal law only when and to the extent that it must—i.e., when federal law preempts it.”²¹

A license is considered a “general intangible,”²² and proceeds from the sale of a general intangible, if identifiable, are subject to the security interest just as the license was subject to the security interest.²³ A security interest in the private economic rights represented by a license is also a general intangible that may be perfected prior to transfer of the license.²⁴

B. *The FCC*

The Federal Communications Act of 1934 (FCA) governs communications licenses.²⁵ In the FCA, Congress granted the FCC the authority to regulate the use of public airwaves in the United States.²⁶ The FCC has the exclusive right to grant a license to use the airwaves and to approve a transfer of a license by a licensee.²⁷ The only way for an owner to transfer, assign, or dispose of any rights in an FCC license is through obtaining FCC approval.²⁸ In conformance with these requirements, the FCC has a policy against granting a security interest in a license.²⁹ If the creditor were to foreclose on the license, it could change hands without approval and thus violate 47 U.S.C. 310(d). However, as the FCC has expressly stated, “[a] security interest in the proceeds of the sale of a license does not violate Commission policy.”³⁰

19. § 9-504.

20. § 9-109(c)(1).

21. § 9-109(c)(1) cmt. 8.

22. § 9-408(a). *See also* *MLQ Investors, L.P. v. Pac. Quadracasting, Inc.*, 146 F.3d 746, 749 (9th Cir. 1998).

23. *See MLQ Investors*, 146 F.3d at 749; *State St. Bank & Trust Co. v. Arrow Commc’ns, Inc.*, 833 F. Supp. 41, 48 (D. Mass. 1993).

24. *MLQ Investors*, 146 F.3d at 749.

25. *See* 47 U.S.C. §§ 151-621 (2006).

26. *See* § 301.

27. *See* §§ 301, 310(d); *see also* 47 C.F.R. § 73.1150(a) (2011).

28. *See* 47 U.S.C. § 310(d).

29. *In re Merkley*, 94 F.C.C. 2d 829 (1983), *aff’d*, 776 F.2d 365 (D.C. Cir. 1985).

30. *See In re Cheskey*, 9 FCC Rcd. 986, 987 (1994).

The FCC policy against liens on licenses is a creation of FCC adjudicative action.³¹ Agencies may establish rules through administrative decisions, and these rules have the same legal effect as regulations.³² However, administrative decisions differ in that they are not subject to public comment and fact-specific decisions.³³

The FCC has failed to address the relationship between its rules and Article 9. Because the FCA, as federal law, preempts Article 9, any inconsistency between the two must be resolved in favor of the FCA. Courts have resorted to their own devices to fill gaps in the regulatory framework regarding whether the FCC's rules preempt Article 9 or may be read consistently with Article 9. Subsection 9-109(c) provides that security interests that are subject to any statute of the United States are not subject to this Article *to the extent* that it is preempted.³⁴ The exclusion is not all encompassing. Article 9 remains applicable to those aspects not preempted by federal law and thus serves a gap-filling mechanism.³⁵ This appears to be the intended result since the Code does not apply *only* to the extent it is preempted.

Therefore, the FCC only preempts Article 9 to the extent that the creditor is able to transfer or act upon the license. A creditor cannot obtain a security interest in a broadcast license, nor may a creditor foreclose on the license, as such rights belong to the licensee through the FCC and may not be abrogated by private agreement. The creditor is left with the limited, yet valuable, right of remuneration upon transfer of the license.³⁶

C. *The Bankruptcy Code*

Section 552 of the Bankruptcy Code governs the effect of security interests granted pre-petition on property acquired by the debtor after the filing of a bankruptcy petition.³⁷ Specifically, subsection (a) provides that any "property acquired by the estate . . . after the commencement of the

31. Isenberg & Reisz, *supra* note 1, at 544.

32. See *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 294, (1974).

33. Isenberg & Reisz, *supra* note 1, at 545.

34. U.C.C. § 9-109(c).

35. 8 WILLIAM D. HAWKLAND ET AL., HAWKLAND UCC SERIES § 9-104:2, *available at* Westlaw. See also *In re Ridgely Commc'ns, Inc.*, 139 B.R. 374 (Bankr. D. Md. 1992) (The court held that the FCC prohibits the enforcement of a security interest in an FCC license and whether to permit it is within scope of the FCC. Further, it recognized that an FCC license is a general intangible in which a creditor may perfect a security interest against private parties, but not as against the government or even the debtor for purposes of foreclosure. Thus, a security interest in an FCC license gives limited rights to the secured party as against other private parties.). *Contra In re Tak Commc'ns, Inc.*, 985 F.2d 916 (7th Cir. 1993) (holding that an FCC license cannot serve as collateral and a secured party cannot take security interest in the license).

36. See 47 U.S.C. §§ 301, 304.

37. 11 U.S.C. § 552.

case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.”³⁸ The purpose of invalidating after-acquired property clauses is to further facilitate the debtor’s fresh start, rehabilitation, and reorganization.³⁹

However, subsection 552(b) provides an exception to the general rule that security interests in after-acquired property in bankruptcy are invalid.⁴⁰ The security interest extends to after-acquired property where the security interest extends to the property acquired before the commencement of bankruptcy and to the proceeds of such property acquired post-petition.⁴¹ The Bankruptcy Code does not define “proceeds,” but most courts use the definition provided in the UCC.⁴² Therefore, so long as collateral is part of the bankruptcy estate, the proceeds arising from the sale or transfer of that collateral belong to the secured creditor.

Now that the foundations of the relevant law have been laid, it is appropriate to discuss the issue in the broadcasting context.

III. THE ISSUE

Lenders relying on what was thought to be an acceptable framework when granting security interests in an FCC license may now be at risk. To fully understand the issue, it is helpful to understand how lenders decide whether to lend to a broadcasting entity.

Lenders want an enforceable lien on all of the debtor’s assets to secure their loan but must be careful when those assets include an FCC license, because the lender cannot take an interest in the license itself.⁴³ Lenders generally require assurance that they will be repaid, and to get that assurance, they take a security interest in the debtor’s assets.⁴⁴ Ideally, a debtor’s business is successful, and the debtor is able to repay the lender from its cash flow. However, if the business struggles or fails and the lender can no longer rely on cash flow, the lender can rely on assets

38. § 552(a).

39. See *In re Tracy Broad. Corp.*, 438 B.R. 323, 329 (Bankr. D. Colo. 2010), *aff’d*, 469 B.R. 55 (D. Colo. 2011), *rev’d*, 696 F.3d 1051 (10th Cir. 2012).

40. See 11 U.S.C. § 552(b).

41. *Id.*

42. See, e.g., *In re Bumper Sales, Inc.*, 907 F.2d 1430, 1437 (4th Cir. 1990). See U.C.C. § 9-102(a)(64) (defining proceeds as, “(A) whatever is acquired upon the sale, lease, license, exchange, or other disposition of collateral; (B) whatever is collected on, or distributed on account of, collateral; (C) rights arising out of collateral; (D) to the extent of the value of collateral, claims arising out of the loss, nonconformity, or interference with the use of, defects or infringement of rights in, or damage to, the collateral; or (E) to the extent of the value of collateral and to the extent payable to the debtor or the secured party, insurance payable by reason of the loss or nonconformity of, defects or infringement of rights in, or damage to, the collateral”).

43. See 47 U.S.C. § 310(d); see also *In re Merkley*, 94 F.C.C.2d 829 (1983).

44. LAWRENCE, HENNING & FREYERMUTH, *supra* note 6, at 3.

secured by a security agreement.⁴⁵ In determining how much money to lend, the lender generally reviews the debtor's assets to ensure they are sufficient to secure the loan.

The issue that arises with a broadcasting business is that it is not an asset-based business like a car dealership or a toy store.⁴⁶ Instead, an FCC license is usually a broadcasting entity's largest asset, along with the airtime that the broadcaster sells as a result of having that license.⁴⁷ Trouble arises from the fact that the broadcaster's most valuable asset is its FCC license,⁴⁸ and the FCC limits lenders' ability to take the license as collateral.⁴⁹ As a result, lenders "are often hesitant to lend to broadcasters."⁵⁰ Thus, the FCC policy, while valid, seriously limits broadcasters looking to borrow money.

Also, the inability to secure the monetary value of a license has "created a significant opportunity for mischief at the expense of the creditor."⁵¹ When a broadcasting entity is without a license, the entity's assets, being mostly equipment, basically lose all value.⁵² Thus, broadcasters have been able to threaten their lenders with the idea of having to judicially enforce their liens, which virtually forces lenders into restructuring their debts.⁵³

With three separate policy concerns at play, courts have reached different conclusions regarding the validity of a lien on a government issued license. The heart of the controversy discussed in this article lies in the extent to which the FCC's limit on rights in a broadcasting license preempts Article 9. This article addresses the question of whether an interest should attach to the proceeds of the sale of an FCC license when the sale may not occur until after bankruptcy has been declared.

45. *Id.*

46. Frank Montero, *Security Interest in FCC Licenses: A Key to Unlocking Capital Sources?*, COMMLAWBLOG (Nov. 7, 2008), <http://www.commlawblog.com/2008/11/articles/broadcast/security-interests-in-fcc-licenses-a-key-to-unlocking-capital-sources/>.

47. *Id.*

48. *Id.*

49. 47 U.S.C. § 310(d) ("No construction permit or station license, or any rights thereunder, shall be transferred, assigned, or disposed of in any manner, voluntarily or involuntarily, directly or indirectly, or by transfer of control of any corporation holding such permit or license, to any person except upon application to the Commission and upon finding by the Commission that the public interest, convenience, and necessity will be served thereby.")

50. Montero, *supra* note 46.

51. Isenberg & Reisz, *supra* note 1, at 554.

52. *Id.*

53. *Id.*

IV. THE EVOLUTION OF THE LAW: SECURITY INTERESTS IN FCC LICENSES

Before the FCC clarified its position in *Cheskey*,⁵⁴ discussed in Subpart D of this section, it was generally understood that creditors could not take a security interest in either the license itself or any proceeds arising from the license.⁵⁵ Thus, when a debtor filed for bankruptcy, there were not many assets in the bankruptcy estate from which creditors could be repaid since the FCC license was off limits. Problems also arose when the FCC served as both the licensor-regulator and the secured creditor,⁵⁶ though that issue is outside the scope of this article.

Prior to 1992, it was generally understood that a lien could not be placed on an FCC license. However, that year the issue of whether a lien could be placed on an FCC license arose in two federal court cases that reached opposite conclusions.

A. *The Tak Decision*

In re Tak Communications, Inc. was the first case to address as its central issue the validity of a perfected security interest on a broadcast license.⁵⁷ The secured creditors sought enforcement of a security interest in an FCC license. The security agreement encompassed all of the debtor's tangible and intangible assets, including its FCC licenses, to secure a \$175,000,000 line of credit.⁵⁸ After the debtor filed for Chapter 11 bankruptcy, the lenders instigated an adversary proceeding to declare their liens valid.⁵⁹ The *Tak* court held that the lien on the FCC license was invalid because the "FCC has consistently and unequivocally refused to recognize such interests," citing a 1965 FCC ruling precluding security interests in FCC licenses.⁶⁰

Affirming the bankruptcy court's holding, the United States District Court for the Western District of Wisconsin found that the FCC did not permit security interests in broadcasting licenses and that the security interest in the debtor's FCC license "to the extent that such rights are

54. *In re Cheskey*, 9 FCC Rcd. 986, 987 (1994).

55. *In re Merkley*, 94 F.C.C.2d 829, 830-31 (1983) (holding that a broadcast license is distinguishable from an entity's physical assets, as it is neither an owned asset nor a vested property interest, and therefore an FCC license cannot be subject to a lien).

56. For more on this issue, see *F.C.C. v. NextWave Pers. Commc'ns Inc.*, 537 U.S. 293, 304 (2003) (holding that FCC regulations notwithstanding, § 525 of the Bankruptcy Act precludes the FCC from cancelling a license because the licensee failed to pay a dischargeable installment debt).

57. *In re Tak Commc'ns, Inc.*, 138 B.R. 568, 571 (W.D. Wis. 1992), *aff'd*, 985 F.2d 916 (7th Cir. 1993).

58. *Id.*

59. *In re Tak Commc'ns, Inc.*, 985 F.2d 916, 916-17 (7th Cir. 1993).

60. *Id.* at 918 (citing *In re Twelve Seventy, Inc.*, 1 F.C.C.2d 965, 967 (1965)).

assignable” was unenforceable.⁶¹ The court concluded that the issue of the validity of a security interest in an FCC license was “a matter for the FCC rather than the courts to decide.”⁶²

B. *The Ridgely Decision*

In re Ridgely Communications, Inc. was decided shortly after *Tak* and recognized the inequity of the FCC policy. In *Ridgely*, the debtor owned and operated two commercial radio stations and granted a secured lender a first priority lien on all of its tangible and intangible property.⁶³ Upon filing a Chapter 11 bankruptcy petition, the debtor sold its assets, including the FCC license.⁶⁴ The secured creditor demanded the proceeds from the post-petition sale, but the debtor argued that the lien was invalid as to the FCC license and resulting sale proceeds.⁶⁵

The bankruptcy court agreed with the secured creditor and held that the debtor’s rights under the license were property of the bankruptcy estate.⁶⁶ The court began its analysis by distinguishing between a debtor’s “private right” to receive economic value and the FCC’s “public right” to assign FCC licenses.⁶⁷ The court noted that the FCC’s primary concern was “with preserving its regulatory authority over licensees and over the transfer of broadcast licenses.”⁶⁸ In holding that the perfection of the creditor’s private right in the economic value of the license did not disrupt the FCC’s public right to regulate the license, the court concluded that “a creditor may perfect a security interest in a debtor’s FCC broadcasting license, limited to the extent of the licensee’s proprietary rights in the license vis-a-vis private third parties.”⁶⁹ The court noted that a security interest in the debtor’s private right should not raise any policy concerns, as it does not allow creditors to “initiate an involuntary transfer of the license to the creditor[] or to compel the initiation of a transfer or assignment of a license to a private third party.”⁷⁰ The court was clear in emphasizing that the FCC’s rights cannot be repealed by a private agreement such as a security interest and that the right was limited to “the right of the creditor to claim proceeds

61. *Tak Commc’ns*, 138 B.R. at 577 (emphasis in original).

62. *Tak Commc’ns*, 985 F.2d at 919.

63. *In re Ridgely Commc’ns, Inc.*, 139 B.R. 374, 375 (Bankr. D. Md. 1992).

64. *Id.*

65. *Id.* at 375–76.

66. *Id.* at 378.

67. *Id.* at 378–79.

68. *Id.* at 376 n.1.

69. *Id.* at 379.

70. *Id.*

received by the debtor licensee from a private buyer in exchange for the transfer of the license to that buyer.”⁷¹

The court emphasized the narrow holding in its decision and reiterated that the decision was “not a recognition of a general right of creditors to take blanket security interests in broadcast licenses.”⁷² The court further stressed:

[T]he security interest recognized here [does not] entitle the creditor to “foreclose” on a broadcasting license . . . or to compel the initiation of a transfer or assignment of a license to a private third party. These are rights of the licensee vis-a-vis the F.C.C. and may not be abrogated by private agreement.⁷³

Ridgely presented a viable solution to the problem of granting a security interest in an FCC license by applying Article 9 to the extent it was not preempted by the FCC.

Also, the bifurcation of a licensee’s rights into lienable private rights and non-lienable public rights is well recognized when granting liens on other types of licenses.⁷⁴ For instance, several courts have used this method to permit the attachment of a security interest to the private economic rights of a liquor license.⁷⁵ This is analogous to what is explicitly permitted by Article 9 with state-created licenses.⁷⁶ Because the idea of bifurcating the license into public rights and private rights is not new to the UCC, it should not be in conflict with state UCC provisions and should not be difficult for courts to apply.⁷⁷

For example, assume you are in a state that treats liquor licenses as property and there is a state law providing that liquor licenses are nontransferable without the permission of the state liquor board. Thus, we have a state-created license that is nontransferable without the permission of the liquor board. UCC 9-408(c) explicitly permits a present right in something that will ripen into future value.⁷⁸ Under 9-408(c),

71. *Id.*

72. *Id.*

73. *Id.*

74. *See* U.C.C. § 9-408(c). Many cases have endorsed the ability of a secured lender to take a limited lien on a liquor license. *See* *Hidden Hollow Golf Course, Inc. v. Tittabawassee Inv. Co.* (*In re* *Tittabawassee Inv. Co.*), 831 F.2d 104 (6th Cir. 1987); *O’Neill v. Dorothy* (*In re* *O’Neill’s Shannon Vill.*), 750 F.2d 679 (8th Cir. 1984); *Kluchman v. N. Side Deposit Bank* (*In re* *Kluchman*), 59 B.R. 13 (Bankr. W.D. Pa. 1985); *In re Bennett Enters., Inc.*, 58 B.R. 918, 919–20 (Bankr. D. Ma.1986).

75. *See, e.g., In re Kluchman*, 59 B.R. at 15 (holding that even though the license cannot be foreclosed upon and sold, a security interest can attach to the private economic rights held by the debtor, including the right to receive cash proceeds from an authorized sale or transfer of the license.).

76. *See* U.C.C. 9-408(c).

77. *Isenberg & Reisz, supra* note 1, at 558.

78. § 9-408(c).

notwithstanding licensing restrictions, you can grant a security interest in a license without violating state law. However, just as with FCC licenses, the secured party cannot enforce this interest.⁷⁹

The major value is the proceeds received from the license rather than the right to sell liquor itself. Thus, if FCC licenses were state-created licenses, Article 9 would override, even if the licensor prohibited transfers of the license. Further, the UCC provides an example of how the rights function in the bankruptcy context.⁸⁰ Thus, the right is not too remote to constitute a property right for purposes of attachment. The UCC readily recognizes present rights in something that will not ripen into something of value until a future date, as shown by the analogy provided in Section 9-408.⁸¹

C. *The FCC Declaratory Ruling*

In 1994, the FCC issued a declaratory ruling in *In re Cheskey* to resolve the conflict highlighted by *Tak* and *Ridgely* and recognized that “[a] security interest in the proceeds of the sale of a license does not violate Commission policy.”⁸² The FCC explicitly adopted the public and private rights distinction articulated in *Ridgely*: “If a security interest holder were to foreclose on the collateral license, by operation of law, the license could transfer hands without the prior approval of the Commission. In contrast, giving a security interest in the proceeds of the sale of a license does not raise the same concerns.”⁸³ The FCC concluded that the *Tak* court erred in its reasoning and noted that “[t]he court’s ruling cannot bind the Commission to a policy which it does not have.”⁸⁴

After *Cheskey*, it was clear that a security interest in the proceeds of the sale of a license was not offensive to FCC policy.⁸⁵ *Cheskey* emphasized the distinction between an unlimited security interest in a broadcast license and a security interest in the proceeds of the license.⁸⁶ The former potentially allows a creditor to interfere with the FCC’s regulatory

79. § 9-408(d).

80. § 9-408 cmt. 7, ex. 4 (“Under this section . . . the security interest would attach to the franchise. As a result, the security interest would attach to the proceeds of any sale of the franchise while a bankruptcy is pending. However, this section would protect the interests of the [licensor] by preventing the secured party from enforcing its security interest to the detriment of the [licensor].”)

81. Note that U.C.C. § 9-408(c) does not apply only because there is preemptive federal law in this case. However, this section provides a strong analogy to how the majority of courts treat a security interest in an FCC license.

82. *In re Cheskey*, 9 FCC Rcd. 986, 987 (1994).

83. *Id.* at 987.

84. *Id.* at 987 n.8.

85. *Id.* at 987.

86. *Id.*

functions, whereas the latter poses no such risk.⁸⁷ Through *Cheskey*, the FCC defined the extent to which it preempts Article 9.

The FCC's decision was based on sound reasoning and did not hamper the Commission's policy. When a debtor licensee gives an interest in the proceeds of the sale of his FCC license, the creditor has rights regarding the money or assets the debtor received in exchange for the license.⁸⁸ The FCC carefully noted that "[t]he creditor has no rights over the license itself, nor can it take any action under its security interest until there has been a transfer which yields proceeds subject to the security interest."⁸⁹ Therefore, when the creditor exercises his security interest, the licensee will no longer be holding the license.⁹⁰

The *Tak* reasoning, grounded primarily on the presumed policy of the FCC, is substantially weakened now that the FCC itself has rejected the holding and disavowed such a policy in *Cheskey*. However, the controversy over collateral rights in broadcasting licenses did not end with *Cheskey*.

D. *The Post-Cheskey State of the Law*

In July 1998, the Ninth Circuit affirmed the reasoning in *Cheskey* and held that a security interest in the proceeds of the sale of a broadcasting license was enforceable in *MLQ Investors, L.P. v. Pacific Quadracasting, Inc.*⁹¹ The court, citing both *Ridgely* and *Cheskey*, recognized that the security interest attached to the proprietary right in proceeds from the sale of the FCC license.⁹² Consequently, the secured creditor defeated the IRS tax lien.⁹³ After *MLQ Investors*, a creditor could rest slightly more assured that the security interest would be enforceable so long as the security agreement and financing statement clearly included general intangibles, referred to the license as an item of collateral to the extent permitted by law, and was duly perfected prior to any bankruptcy filing.⁹⁴ Thus, the Ninth Circuit recognized that proceeds of the sale of a broadcast license were "general intangibles" and "therefore subject to perfection prior to sale."⁹⁵

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.* See also *In re Ridgely*, 139 B.R. 374 (Bankr. D. Md. 1992). *Contra Tak Commc'ns, Inc.* 985 F.2d 916 (7th Cir. 1993).

91. *MLQ Investors, L.P. v. Pac. Quadracasting, Inc.*, 146 F.3d 746 (9th Cir. 1998).

92. *Id.* at 748-49.

93. *Id.* at 749.

94. *Id.*

95. *Id.*

David Isenberg and Michael Reisz explained, “the best reading of existing FCC authority establishes that the FCC has never ruled squarely on the issue of a limited lien on proceeds of general intangibles.”⁹⁶ However, the FCC has held that licensees have property rights in a license’s private economic value.⁹⁷ As noted by Isenberg and Reisz, where there is no direct bar on such liens, “the validity of such liens should be assumed.”⁹⁸ The authors further argued that if the state law is not preempted, then there is no reason to treat licenses any differently than other articles of collateral.⁹⁹

The resolution remains ambiguous under existing FCC authority, despite the *Ridgely* and *Cheskey* decisions. Isenberg and Reisz credit this ambiguity “to the fact that the FCC has elected to address the question of security interests through a series of fact-specific administrative adjudications, rather than through the more orderly and disciplined regulatory rule-making process.”¹⁰⁰

V. THE CROSSROADS IN THE LAW TODAY

The approach articulated in *Ridgely* and adopted by *Cheskey* has become the standard method for taking a security interest in the proceeds of a license sale. Since *Cheskey*, courts have deemed it settled law that “a creditor may perfect a lien in the private economic value of an FCC license to the extent that such lien does not violate the FCC’s public right to regulate license transfers.”¹⁰¹ The secured creditor has no right to control or repossess the license. However, the creditor is left with whatever proceeds might arise from a post-default transfer of the license approved by the FCC.

The same issue that arose in 1992 has recently resurfaced. Two federal courts have released conflicting opinions regarding whether a security interest in the proceeds of an FCC license survives bankruptcy.¹⁰²

A. *The Tracy Decision*

In October 2010, the U.S. Bankruptcy Court for the District of Colorado in *In re Tracy Broadcasting Corp.* considered whether a creditor’s security interest extended to “proceeds” of a future transfer of the

96. Isenberg & Reisz, *supra* note 1, at 559 n.81.

97. *Id.*

98. *Id.*

99. *Id.* (citing *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120, 129 (1945) (holding that the state court had the authority to address issues not within the exclusive jurisdiction of the FCC)).

100. See Isenberg & Reisz, *supra* note 1, at 559.

101. *In re TerreStar Networks, Inc.*, 457 B.R. 254, 264 (Bankr. S.D.N.Y. 2011).

102. See *id.*; *In re Tracy Broad. Corp.*, 438 B.R. 323 (Bankr. D. Colo. 2010), *aff’d*, 469 B.R. 55 (D. Colo. 2011), *rev’d*, 696 F.3d 1051 (10th Cir. 2012).

debtor's interest in an FCC license where there was no contract for transfer of the license in existence at the time the Chapter 11 petition was filed.¹⁰³

Prior to filing its bankruptcy case, the debtor obtained a loan from the bank and granted the bank a security interest that included the debtor's "general intangibles."¹⁰⁴ The parties agreed that the bank did not have a valid security interest in the license itself.¹⁰⁵ The issue, however, was whether "the Bank's security interest extend[ed] to 'proceeds' received by the Trustee upon a future transfer of the Debtor's interest in the FCC license, where there was no contract for transfer of the license in existence at the time the Chapter 11 petition was filed."¹⁰⁶ In considering cross-motions for summary judgment, the court held that the proceeds of an FCC license were not subject to a creditor's security interest.¹⁰⁷

The court deemed it "settled law" that an FCC license was distinguishable from a station's physical assets, as it was not subject to any security interest.¹⁰⁸ The court also observed that the license provided for the use of the spectrum but did not convey ownership beyond the terms of the license itself.¹⁰⁹ The court was concerned that the foreclosure of the security interest and transfer of the licenses would occur without FCC approval,¹¹⁰ thus violating 47 U.S.C. § 310(d).¹¹¹

The court addressed the cases that have recognized a limited right of the license holder to grant a security interest in the proceeds of an FCC-approved license transfer to a third party and presumed it was *possible* for a security interest to extend to the proceeds of an FCC license without infringing on the FCC's regulatory power.¹¹² However, the court carefully noted that the FCC has not yet ruled on the issue and that "there are Circuit Court cases which seem to reject any security interest in any aspect of an FCC license."¹¹³

The court proceeded to distinguish proceeds from after-acquired property in bankruptcy.¹¹⁴ Anything received by the debtor resulting from a post-petition transfer of the FCC license could not be "proceeds" under the

103. *Tracy Broad.*, 438 B.R. 323.

104. *Id.* at 325.

105. *Id.*

106. *Id.*

107. *Id.*

108. *Id.* at 327.

109. *Id.* at 328.

110. *Id.*

111. 47 U.S.C. § 310(d) (2006) (providing that "[n]o . . . station license, or any rights thereunder, shall be transferred, assigned, or disposed of in any manner, . . . to any person except upon application to the Commission").

112. *Tracy Broad.*, 438 B.R. at 328.

113. *Id.* at 328.

114. *Id.* at 329.

UCC because the license itself could not be “collateral.”¹¹⁵ Thus, the property acquired from such transfer must fall under after-acquired property.¹¹⁶ The court stated, “[i]f there is no security interest in the property itself, . . . there can be no security interest in any ‘proceeds’ thereof, because there is no disposition of ‘collateral.’”¹¹⁷

The court ignored the use of “general intangibles,” which would have affected the abovementioned analysis, and held:

The Debtor’s right to receive value for a transfer of its License did not exist prior to the filing of its Chapter 11 case because any such “right” was too remote and was subject to two contingencies. . . . First, the Debtor would have to have an agreement to transfer the License, and second, the transfer would have to be approved by the FCC.¹¹⁸

Relying on Section 552 of the Bankruptcy Code, the court granted the plaintiffs’ motion for summary judgment and concluded that the bank’s security interest cannot encumber any value received from any future transfer of the license.¹¹⁹ The court held that, even assuming a limited property right existed, the debtor did not have sufficient rights in the collateral or the power to transfer rights in the collateral pursuant to Section 9-203 of the UCC.¹²⁰ The court thus reasoned that the security interest never attached.¹²¹

The court read the UCC and Bankruptcy Code provisions very narrowly, and the U.S. District Court for the District of Colorado affirmed the bankruptcy court’s rigid holding.¹²² After *Tracy*, agreements relying on what had been the accepted framework when granting interests in the future proceeds of an FCC license may be at risk.

B. *The TerreStar Decision*

Less than a year after the decision in *Tracy*, the U.S. Bankruptcy Court for the Southern District of New York applied what had been considered the standard approach since *Cheskey* in *In re TerreStar Networks*. The court provided the lender with a security interest in the “proceeds” of an

115. *Id.* at 330.

116. *Id.*

117. *Id.* at 329.

118. *Id.* at 330.

119. *Id.* at 330–31.

120. *Id.* at 330.

121. *Id.*

122. *See Valley Bank & Trust Co. v. Spectrum Scan, LLC (In re Tracy Broad. Corp.)*, 469 B.R. 55 (D. Colo. 2011).

FCC license sale and held that a valid security interest existed in the economic value of an FCC license.¹²³ In so doing, the court explicitly rejected the *Tracy* decision.¹²⁴

In *TerreStar*, the security agreement included all license rights, “including, without limitation, the right to receive monies, proceeds, or other consideration in connection with the sale, assignment, transfer, or other disposition of any FCC Licenses, the proceeds from the sale of any FCC Licenses or any goodwill or other intangible rights or benefits associated therewith,” carefully carving out the FCC license itself from the lien.¹²⁵

The court acknowledged the FCC policy that no rights may be granted in an FCC license and recognized that “case law makes clear that, while a lien cannot exist on the license itself, a security interest may attach to the economic value of an FCC license.”¹²⁶

The court followed *Cheskey* and bifurcated the rights in the FCC license.¹²⁷ In reaching its conclusion, the court examined the language of the security agreement and observed that it “[gave] the broadest grant possible over the right to receive economic value from an FCC License.”¹²⁸ The court solidified its reasoning when it noted that even if Section 552(a) of the Bankruptcy Code applied, as conflicting decisions such as *Tracy* contended, the lien would fall within the exception provided in Section 552(b).¹²⁹ Thus, the lien would be valid.¹³⁰

The court recognized that since the *Cheskey* decision, “it appears to be settled law that a creditor may perfect a lien in the private economic value of an FCC license to the extent that such lien does not violate the FCC’s public right to regulate license transfers.”¹³¹

The court described the *Tracy* decision as “problematic,” as it based its conclusion on the “faulty assumption that ‘there has been no definitive ruling from the FCC itself, and there are Circuit Court cases which seem to reject any security interest in any aspect of an FCC License.’”¹³² The court further criticized *Tracy* for citing *Tak* for this proposition, as the FCC

123. *In re TerreStar Networks*, 457 B.R. 254 (Bankr. S.D.N.Y. 2011).

124. *Id.* at 269.

125. *Id.* at 258 (emphasis omitted).

126. *Id.* at 262.

127. *Id.* at 265.

128. *Id.*

129. Section 552(b) provides that a valid prepetition lien in property can extend to value generated by such property post-petition when expressly provided for in the security agreement. *Id.* at 270 n.14.

130. *Terrestar*, 457 B.R. at 269–70 n.14.

131. *Id.* at 264 (citing *MLQ Investors, L.P. v. Pac. Quadracasting*, 146 F.3d 746, 748 (9th Cir. 1998)).

132. *Id.* at 269.

explicitly rejected that reasoning in *Cheskey* on grounds that it was “inconsistent with FCC policy.”¹³³

The court also discredited *Tracy*’s reliance on *Sims* by noting that the decision was issued before “general intangibles” were included as a type of collateral under the UCC.¹³⁴ Although *Tracy*’s reasoning is flawed for many reasons, *Terrestar* missed the mark on this criticism, as general intangibles have always been a part of the UCC.¹³⁵ Despite the court’s misunderstanding of the history of general intangibles, the court otherwise presented valid criticisms of the reasoning in *Tracy*.

The court further described the *Tracy* decision as “fundamentally at odds” with case law and noted that it ignored “the sound reasoning” of *Ridgely* in recognizing the distinction between public and private rights associated with an FCC license.¹³⁶ The court cautioned that accepting the *Tracy* decision “would unsettle expectations by invalidating such liens in the bankruptcy context or permitting all other creditors to come before the liens, thus severely diminishing or eliminating their value.”¹³⁷

Although these two conflicting decisions appear to be immaterial at first glance, their contradictory outcomes rock the boat for those lending to broadcasting entities. Now, secured creditors should be prepared for a debtor to argue that security interests in the proceeds of a license sale are precluded by Section 552 of the Bankruptcy Code. Although *TerreStar* provides a valid counter argument, *Tracy* stands for the proposition that it is not the winning argument creditors once thought it to be.

VI. CONCLUSION

The *TerreStar* court applied the better-reasoned view and correctly concluded that a security interest in the proceeds of a post-petition license transfer is valid. The current state of the law does not reduce enforcement costs on liens. Instead, it increases litigation and uncertainty while decreasing the number of lenders willing to lend to broadcasting entities.

Tracy reached the wrong conclusion for many reasons. First, contrary to the *Tracy* court’s assumption, the FCC ruled on this particular issue in

133. *Id.*

134. *Id.*

135. See U.C.C. § 9-106 (1962) (defining “general intangibles” as “any personal property (including things in action) other than goods, accounts, contract rights, chattel paper, documents and instruments”). The source the court relied upon explains the treatment in 1962 of accounts, contract rights, and general intangibles. See 8 HAWKLAND, *supra* note 35, at § 9-106:1. The contract rights category was deleted from the UCC in 1972 and assets that were formerly contract rights became either accounts or general intangibles. Ray D. Henson, *A Problem Involving Assignments of Accounts Under Article 9*, 40 WASH. & LEE L. REV. 41, 42 (1983).

136. *TerreStar*, 457 B.R. at 269.

137. *Id.* at 269–70.

Cheskey. Second, the court in *Tracy* relied on *Tak*, which the FCC explicitly rejected in *Cheskey* as misconstruing FCC policy. A wide acceptance of *Tracy* would render the FCC ruling in *Cheskey* meaningless. Third, ignoring the distinction between public and private rights in an FCC license, the reasoning in *Tracy* creates two conditions on the attachment of a lien against the economic value of a broadcast license and concludes that an interest that does not satisfy these conditions is too remote to constitute a property right. *Tracy*'s rationale incorrectly hinges on the idea that the interest never attached. However, the UCC readily recognizes property rights in things that will not ripen into something of value until a future date.¹³⁸

Finally, *Tracy* is problematic because it decreases the certainty with which lenders may proceed under the UCC and thereby directly contradicts the UCC's stated purpose. Accepting *Tracy* would unsettle expectations and diminish the value of liens against the value of an FCC license in the bankruptcy context. The Colorado Bankruptcy Court's decision in *Tracy* is merely an outlier. Other than that isolated decision, "courts have uniformly recognized that an FCC license is a general intangible and that a lien on such an intangible may be perfected prepetition before any proceeds or other consideration is generated and prior to any transfer, sale, or other disposition of the license."¹³⁹

The *TerreStar* approach is more viable, as it is in accord with the extent of FCC preemption of Article 9. It also is aligned with the Bankruptcy Code. When the license is sold, the existing security interest is liquidated, thereby avoiding the effect of Section 552. The weight of authority suggests that such liens are permissible. In permitting an enforceable lien on the proceeds of the sale, transfer, or assignment of a license, *TerreStar* merely endorsed what had become a well-established practice not only in the broadcasting industry but also in other areas of governmental licensing, such as liquor licensing. Although the *TerreStar* decision provided a remedy for the immaterial hurdles *Tracy* created (prepetition FCC approval and sale), these conflicting decisions leave creditors wary of taking security interests in FCC licenses.

The recognition of valid attachment of security interests to private rights of an FCC license is consistent with FCC policy, which only prohibits liens on the public operational rights in a license. However, ambiguity remains, and we will continue to see decisions like *Tracy* unless the FCC resorts to the rulemaking process to clarify what has been muddled by various courts' interpretations of the extent to which the FCC

138. See U.C.C. § 9-408(c); see also *supra* notes 71–79 and accompanying text discussing security interests in liquor licenses.

139. *TerreStar*, 457 B.R. at 266.

preempts Article 9. Both borrowers and lenders would welcome greater clarity on this issue. The likely result of greater clarity would be increased lending to broadcasters, since lenders would be able to draft security agreements with greater certainty.

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