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The Road Map for Potential Foreign Investors in Broadcast Stations

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Restrictions on foreign ownership of broadcast stations have been in effect for over 100 years. As a result of initiatives taken during former FCC Chairman Tom Wheeler's tenure to spur foreign investment and the composition of the current FCC under President Trump, the time has never been better for broadcasters to obtain foreign investment in their stations that will pass muster with the Commission.

The Statutory Law in a Nutshell

Section 310(b)(3) of the Communications Act specifies that the Commission may not grant a broadcast application to a proposed licensee of which more than 20% of the equity is directly owned of record or voted by non-US citizens (including those holding "green cards"), a foreign government, or an entity organized under the laws of a foreign country (referred to in the Communications Act as "aliens"). The FCC has no statutory authority to allow direct foreign investment in a broadcast licensee in excess of this 20% cap.

In contrast to the statutory limit on direct foreign ownership of a broadcast license, Section 310(b)(4) specifies that, if a proposed broadcast licensee is directly or indirectly controlled by a holding company, the Commission may refuse to grant a license to that proposed licensee if more than 25% of the capital stock of the holding company will be owned of record or voted by aliens and if the FCC finds that the public interest will be served by a refusal to grant the broadcast license. Historically, FCC public interest determinations to allow indirect foreign investments in broadcast properties in excess of 25% have been extremely rare, and as a result, both broadcasters and foreign investors had considered 25% to be a de facto cap on indirect foreign ownership of U.S. radio and television stations.

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2013 FCC Declaratory Ruling

In an effort to remove uncertainty surrounding the limitations on foreign investment in broadcast licenses, the FCC issued a Declaratory Ruling in 2013 announcing that the 25% statutory benchmark is not immutable. Thus, the FCC will consider whether indirect foreign voting or equity ownership interests exceeding 25% would serve the public interest based on the unique facts of each case, taking into account public interest and national security considerations. Broadcasters have been afforded considerable flexibility to request foreign ownership approvals tailored to their unique circumstances. For example, they are now able to request: (1) approval of up to and including 100% aggregate foreign ownership (voting and/or equity) by unnamed and future foreign investors in the controlling U.S. parent of a broadcast licensee, subject to certain conditions; (2) approval for any named foreign investor that proposes to acquire a less than 100% controlling interest to increase the interest to 100% at some future time; and (3) approval for any non-controlling named foreign investor to increase its voting and/or equity interest up to and including a non-controlling interest of 49.99% at some future time.

More recently, the FCC adopted "streamlined" procedures for obtaining approval to exceed the 25% benchmark on indirect foreign ownership. The Commission heralded this action as designed to lower costs and regulatory burdens and to "facilitate investment from new sources of capital at a time of growing need for investment" in broadcasting. Chairman Tom Wheeler hailed the Declaratory Ruling as furthering the goals of the FCC's Spectrum Incentive Auction:

"Today's ruling could, for example, unleash new capital to help stations to make the up-front investment necessary to share a channel after their spectrum is sold at auction. Similarly, foreign capital that would help a broadcaster move from the UHF band to VHF band might also further the Commission's efficiency goals. We are in the midst of a major effort to improve spectrum efficiency, and I encourage those who might want to attract foreign investment to keep those goals in mind."

Growing Interest in Foreign Interest in Acquiring Media Properties

Continuing trends regarding foreign investment in the U.S. provide optimism for fulfillment of the FCC's vision. Investment in the U.S. by foreign commercial enterprises remains strong, with China and the U.K. leading the way as the most prominent foreign investors in the U.S. technology, media and technology sector. For example, China's Dalian Wanda Group has announced its intention to acquire Dick Clark Productions, a TV production company for $1 billion, giving it the broadcasting rights to the Golden Globe Awards, the Academy of Country Music Awards and the New Year's Eve countdown celebrations in New York City. Similarly, the second largest telecom company in France recently agreed to pay approximately $26.8 billion to acquire Cablevision and Suddenlink, creating the fourth largest cable company in the U.S.

Impact of FCC Efforts

There are positive signs that the FCC reforms are beginning to attract additional foreign investment in U.S. broadcast properties. In 2015, the FCC authorized Pandora Media ("Pandora"), parent company of the licensee of a radio station in Box Elder, South Dakota, to have levels of foreign ownership (voting and equity) in excess of the 25% benchmark. However, the approval contained several conditions, including a requirement that FCC permission be obtained before aggregate foreign ownership could exceed 49.99 percent. More recently, the FCC granted a request by Corvex Master Fund LP, an entity organized in the Cayman Islands but ultimately controlled by U.S. citizens, to exercise stock options that would increase its 4.95% voting and equity interests in Pandora to 9.99%, and ultimately up to 14.99% in the future, without further FCC approval.

In another recent decision, the FCC authorized Univision Holdings, Inc., in connection with an anticipated initial public offering of its common stock, to have an aggregate foreign investment (equity and voting) of up to 49%, including up to a 40% equity and voting interest to be held by Grupo Televisa, S.A.B., a Mexican company that is an existing investor in, and business partner of, Univision.

This case is significant, if nothing else, due to the sheer size of Univision. With approximately 60 television licenses (full power, LPTV and translator) and 75 AM and FM radio stations, Univision is among the nation's largest broadcast companies. And while Televisa requested a 40% stake in Univision, and thus would not hold de jure control, it seems evident that it intends to maintain its substantial involvement with Univision, e.g., as exclusive, long term U.S. broadcast and digital rights holder to Televisa's Spanish language programming. Notably, in its Univision/Televisa decision, the FCC made no mention of the past history of foreign ownership violations involving Univision's attributable principles. See, e.g., Spanish International Communications Corporation, 2 FCC Rcd 3336 (1987).

On the heels of the Univision decision, the FCC granted a request by Hemisphere Media Group, Inc., which indirectly owns the licensee of three television stations in Puerto Rico, to increase its foreign ownership by specified Mexican entities and individuals up to 49.99% in the aggregate, subject to certain monitoring, reporting and compliance requirements. Even more recently, the FCC issued a Declaratory Ruling authorizing husband/wife Australian citizens to raise their indirect ownership from 20% to 100%, through Frontier Media, LLC, in entities holding 29 broadcast station licenses. This situation involved numerous factors favoring the applicants: long term (10 year) U.S. residency, substantial experience in broadcast management, and citizenship from one of the closest allies of the U.S. Nevertheless, the case is significant in that it is the first time for FCC approval of 100% indirect foreign ownership of a broadcast licensee.

Downsides to FCC Approval Process

While recent FCC efforts to facilitate the process for obtaining a public interest determination to exceed the 25% benchmark on indirect foreign ownership in broadcast properties are clearly helpful, certain drawbacks remain.

Delay

The Pandora request discussed above took over two years for the FCC to decide, and the Univision case was pending at the agency for over a year. Although the recent FCC streamlining order may help expedite matters, the fact-based, case-by-case analysis remains inherently time consuming. A seller with desirable broadcast properties may simply be unwilling to wait for FCC approval of potential foreign investors.

Subject to external forces

The FCC has confirmed that any request to exceed the 25% benchmark on indirect foreign ownership continues to be subject to concurrent review by “Team Telecom,” i.e., various federal agencies charged with national security: the Departments of Homeland Security, Defense, Justice, State, Treasury and Commerce, as well as the U.S. Trade Representative and the FBI. Not only is such review not subject to time constraints or procedural safeguards, it lacks precedential guidance for future applicants on acceptable or unacceptable foreign ownership arrangements and raises the possibility for behind-the-scenes political influences from multiple sources.

Uncertainty

Significantly, neither the 2013 Declaratory Ruling nor the more recent procedural streamlining order provides substantive guidance as to whether a particular proposal for indirect foreign ownership will be granted. Rather, the FCC merely reiterated that it will continue to evaluate public interest factors raised by each individual request, including the goals of encouraging investment, innovation, media diversity, localism, and the efficient use of spectrum.

Given the dearth of FCC precedent, potential investors are left with scant guidance on whether a particular foreign ownership proposal might pass muster. By contrast, FCC decisions involving common carrier licenses have been far more common, and many such applications are now routinely granted. The FCC regards common carrier licenses, which typically involve passive transmission of third party information, as being unlike broadcast stations that provide a potential outlet for foreign propaganda. Thus, as then Chairman Wheeler emphasized in connection with the 2013 Declaratory Ruling, while the FCC is “open to considering” proposals for indirect foreign ownership in broadcast stations in excess of 25%, “this is far from an indication that we’re going to rubber stamp them.”

Other Options for Foreign Investors

For foreign investors finding the FCC approval process to be daunting, it should be noted that numerous other avenues remain open for participation by foreign investors in the U.S. broadcast media without the necessity of prior FCC approval. However, pursuit of any of these options must be implemented with extreme care to remain compliant with applicable FCC requirements.

Participation as Officers or Directors

Due to a 1996 amendment to the Communications Act, there is much greater flexibility for foreign nationals to serve as officers or directors of a corporation holding a broadcast license or its parent entity, even if such individuals also hold equity ownership interests within the applicable caps. Naturally, among other safeguards, care must be taken to ensure that such participation by foreign officers or directors does not precipitate a transfer of control of any broadcast license.

Maximization of Stock Holdings

Even within the 20% and 25% caps on stockholdings by non U.S. citizens, certain mechanisms can be utilized by foreign investors to maximize their interests if properly structured. For example, there is no "flow through" of holdings falling within the separate 20% limit on direct stock ownership and the 25% cap applicable to indirect interests. Thus, the same foreign individual can hold up to 20% in the licensee itself and also hold up to 25% in the licensee's parent corporation.

Similarly, in situations where numerous intermediate entities may hold separate minority or non-attributable interests in a broadcast licensee, the FCC uses a "multiplier" approach to calculate compliance with the foreign ownership limits. Thus, for example, a non U.S. citizen might hold a 60% interest in a properly-insulated limited partnership that owns 30% of the equity in an entity holding a broadcast license. Using the multiplier, the foreign interest would be 18% (60% x 30%), well within the statutory benchmark.

Preferred Stock

While all classes of stock (including non-voting) are subject to the applicable 20% and 25% limits on direct and indirect foreign ownership, a foreign investor may be able to obtain increased protections or returns through preferred stock that might be more secure, e.g., in the event of bankruptcy, or that could pay higher dividends than common stock.

Minority Shareholder and Creditor Protections

Even if a foreign investor holds the maximum amount of stock under the applicable benchmarks, the FCC generally allows various minority shareholder protections. For example, properly structured covenants might provide for minority shareholder approvals of certain extraordinary corporate actions, such as a merger or sale of significant assets, dilution of stock, or major changes in lines of business.

Trusts

Interests held in a properly structured trust are generally not attributable under FCC rules. Thus, a foreign investor who is the beneficiary of a trust might realize greater potential gain by holding in trust any interests in excess of the statutory benchmark, with the future ability to either sell such interests to a qualified purchaser or hold such interests directly upon obtaining any necessary FCC approval.

Convertible Instruments

The FCC generally does not consider convertible interests, such as warrants, debentures or options, held by non U.S. citizens to be covered by the statutory foreign ownership restrictions unless and until such interests are actually converted to equity. Thus, as with the trust mechanism described above, a foreign investor might hold interests that are convertible to equity holdings exceeding the statutory benchmarks and later sell such interests to a U.S. citizen or seek appropriate FCC approval to directly hold such interests upon conversion.

Debt

There are no limitations on the provision of debt financing by foreign lenders to entities holding U.S. broadcast licenses. And while such loans can be entered into without the need of FCC approval, care must be taken to ensure that the debt will not be deemed to be equity by the Commission, for example, because the lender is permitted to become overly involved in the operation of the enterprise or the debt is a substantial portion of the licensee's capitalization.

Contractual Arrangements

Finally, foreign entities can participate in the U.S. broadcasting market through appropriate contractual arrangements, such as the supply of programming, advertising sales, local marketing agreements or similar arrangements. Moreover, such contracts might be coupled with equity ownership within the applicable benchmarks. Again, care must be taken to avoid excessive involvement in management so as to trigger transfer of control concerns.

The Trump FCC Strongly Favors Foreign Investment in Broadcast Stations

The current composition of the FCC augurs well for broadcasters seeking an infusion of capital from foreign investors without running afoul of FCC regulations. Chairman Ajit Pai has gone on record as saying that while the 2013 Declaratory Ruling was a good first step, the Commission must go further. Commissioner Michael O'Rielly also believes the FCC's 2013 Declaratory Ruling does not go far enough and that the Commission should either establish a higher cap before requiring agency approval, such as 49% or 74%, or by shifting the burden onto the FCC to justify a prohibition of foreign investment rather than requiring the Commission's affirmative approval. Commissioner Mignon Clyburn supports loosening of restrictions on foreign ownership of broadcast stations as a means of encouraging greater diversity of ownership, observing that "competition and innovation in media in the 21st century move at warp speed, and in order to keep pace, broadcasters need new and increased sources of capital."

Suggested Timing for Next Steps

We recommend that broadcasters and potential foreign investors not wait until an investment opportunity arises before they consider the options presented by the FCC's more flexible approach. For broadcasters, by delaying until they face a pressing need to raise capital or possibly sell, they may be foregoing more favorable financial outcomes if they neglect to pave the way for foreign investment. Similarly, potential foreign investors may be precluded from attractive opportunities to achieve ownership stakes in broadcast properties due to the delays inherent in failing to obtain advance approval, particularly when evaluated against other potential bidders.