No. 07-803

IN THE
Supreme Court of the United States

DONALD A. THACKER, TRUSTEE,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION AND UNITED STATES OF AMERICA,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF

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MISCELLANEOUS

Recycling arguments from *NextWave*, the FCC contends that it may shift between "separate and independent" powers as creditor and regulator according to its immediate pecuniary advantage. By ratifying the FCC's exploitation of its hybrid status, the decision below created an acknowledged circuit split with the D.C. Circuit's opinion in *NextWave* and clear tension with this Court's *NextWave* decision, and overturned the expectations of private actors relying on long-established rules of commercial law. This Court should grant review to determine the correct approach to analyzing agency conduct in this kind of hybrid program, and to put an end to the FCC's misuse of its regulator status to circumvent its obligations under debtor-creditor law.

ARGUMENT

1. The FCC cannot explain away the D.C. Circuit's holding in *NextWave* that license cancellation for nonpayment of a debt in these circumstances is also a lien-enforcement action. *NextWave Personal Commc'ns Inc. v. FCC*, 254 F.3d 130, 151 (D.C. Cir. 2001), *aff'd*, 537 U.S. 293 (2003); *see also NextWave Personal Commc'ns Inc. v. FCC*, 537 U.S. 293, 320 (2003) (Breyer, J., dissenting) ("In these very cases, the Government sought to retake its licenses through enforcement of the security interest"). The FCC tries to distinguish the D.C. Circuit's holding by arguing that Magnacom, unlike NextWave, consented to lifting the automatic stay under § 362 of the Bankruptcy Code. But neither the D.C. Circuit's holding that cancellation for nonpayment is a lien-enforcement action, nor the Ninth Circuit's contrary ruling, turned on whether

the debtor consented to lift the stay. Nor would that make any sense. As the D.C. Circuit observed, 254 F.3d at 155, the automatic stay *prohibits* lien-enforcement actions against a bankruptcy debtor *unless* it is lifted. *See* 11 U.S.C. § 362(a)(4), (5). Indeed, in this case the bankruptcy court based its lift-stay order on provisions that allow a secured creditor to enforce its lien or security interest. *See* Pet. 8; 11 U.S.C. § 362(d)(1), (2). Thus, far from negating the lien-enforcement character of the FCC's cancellation, lifting the stay was the *precondition* for the lien enforcement to proceed lawfully.[1]

Nor is there merit to the FCC's suggestion that the D.C. Circuit's lien-enforcement ruling was somehow limited to the facts of that case. There is no material difference between the license cancellation here and in *NextWave*. In both cases, the licenses were cancelled pursuant to 47 C.F.R. § 1.2110(g)(4) and the FCC's security agreement solely because the licensees failed to pay their secured debts to the FCC.

Like the Ninth Circuit, the FCC belittles the D.C. Circuit's lien-enforcement holding as a drive-by ruling on an issue that was not briefed and argued. Nothing could be further than the truth. The FCC's violation of the automatic stay was raised before the

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[1] Nor does Magnacom's consent to lifting the stay alter the debtor's entitlement to the surplus proceeds under secured-credit law. *Catalano v. Comm'r*, 279 F.3d 682, 686 (9th Cir. 2002) ("Relief from an automatic stay entitles the creditor to realize its security interest … in the property, but all proceeds in excess of the creditor's interest must be returned to the Trustee") (quotation marks omitted).

D.C. Circuit in *NextWave* as an independent ground for setting aside the cancellation, *see* 254 F.3d at 149, and the applicability of the stay was extensively briefed and argued in that court.[2] The D.C. Circuit ultimately resolved the case under § 525, but the FCC's own arguments compelled the court to address the applicability of the automatic stay in the course of that ruling. *Id.* at 150 ("the Commission urges us to read section 525 in light of section 362"). And the court had the full benefit of the parties' extensive briefing in ruling that the automatic stay applied to the regulatory license cancellation precisely because it was also a lien enforcement action.[3] The careful attention given by the D.C. Circuit on this question refutes any suggestion that that court did not regard the issue as necessary to its judgment. In reaching the opposite conclusion, the Ninth Circuit simply disagreed, making this case appropriate for this Court's review.

2. Equally unavailing is the FCC's attempt to explain away the palpable tension between the opinion below and this Court's *NextWave* decision. The FCC erroneously contends that this Court's decision in *NextWave* is irrelevant to the agency's exploitation of its overlapping regulator and creditor

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[2] *See, e.g.*, Brief of Respondents/Appellees, *NextWave Personal Commc'ns Inc. v. FCC*, No. 00-1402, at 16-20 (D.C. Cir. filed Jan 17, 2001).

[3] The D.C. Circuit's meticulous consideration of the automatic stay and lien enforcement issues is also reflected in Judge Tatel's careful application of issue-preclusion principles to establish that these issues remained open. *See* 254 F.3d at 147-49.

roles because the only issue in *NextWave* was interpretation of § 525. That characterization rewrites history by ignoring the agency's own "recurrent theme" in *NextWave*, 537 U.S. at 302, that because cancellation is a regulatory act, it cannot also be a debt collection action. *See* Pet. 27. This Court unequivocally rejected the FCC's "either-or" framing of the case and recognized instead that "a debt is a debt, even when the obligation to pay it is also a regulatory condition." 537 U.S. at 303.

Here, the FCC makes (and the Ninth Circuit adopted) the same argument this Court rejected in *NextWave*. The only difference is that here the applicable body of creditor-debtor law is federal common law governing secured transactions by federal agencies (which presumptively incorporates U.C.C. Article 9). *See* Pet. 30-32; *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 729 (1979). Both in *NextWave* and this case the FCC's position is exactly the same: those laws have no application to license cancellation for failure to pay secured debts to the FCC because such cancellation is a purely regulatory act. *NextWave* rejected that attempt by the agency to game its dual status, whereas the Ninth Circuit condoned it below.

The FCC also suggests in passing that the Court in *NextWave* implicitly approved of the dichotomy between regulatory and creditor actions when it contrasted regulatory "revoking" of licenses with "the enforcement of [a security] interest in the bankruptcy process." Opp. 11 (quoting *NextWave*, 537 U.S. at 307-08). But the Court's point there was that the FCC was not pursuing its remedies "in the

bankruptcy process." *NextWave*, 537 U.S. at 307; *see also id.* at 307 n.5 (noting that FCC "initially participated in the bankruptcy proceedings" but shifted course and claimed authority to unilaterally cancel licenses); Pet. 29 n.14. The Court thus noted that if the FCC were allowed to enforce its rights outside the bankruptcy process, that would create an "anomaly" compared to the rights of ordinary secured creditors. 537 U.S. at 308. It certainly did not resurrect a dichotomy between regulatory and creditor actions that it had previously rejected. *Id.* at 303.

3. In addition to this case and *NextWave*, the Seventh Circuit's recent decision in *In re Airadigm Communications, Inc.*, No. 07-2212, __ F.3d __, 2008 WL 649704 (7th Cir. Mar. 12, 2008), illustrates the way the FCC repeatedly recasts itself either as a creditor or as a regulator – or even, in *Airadigm*, as both simultaneously – according to its immediate litigation interest. *Airadigm* is one more case in which a C-Block debtor-licensee was forced into bankruptcy when the bottom fell out of the spectrum market. *See Airadigm*, 2008 WL 649704 at *2. In the *Airadigm* bankruptcy, the FCC vigorously enforced its rights *as a secured creditor* to obtain priority payment from the bankruptcy estate ahead of the debtor's unsecured creditors. Relying on its lien on the debtor's licenses, the FCC leveraged rights available only to secured creditors to elect a guaranteed stream of payments for the entire amount it was owed while also retaining its lien. *Id.* at *10; *see* 11 U.S.C. §§ 1111(b), 1129(b)(2)(A). Without a security interest in the licenses, the FCC

would have been relegated to the lower payout received by unsecured creditors.

Airadigm thus belies the FCC's contention (Opp. 13) that it demands a security interest in licenses only as a belt-and-suspenders precaution that does not materially alter the parties' rights. As *Airadigm* shows, the FCC's security interest gives it substantial rights that it would not otherwise have – rights that the FCC vigorously enforces whenever it is in the agency's pecuniary interest. The FCC disavows its secured creditor status only where, as here, being a creditor carries obligations the agency wants to escape. *But see Gorden v. Kreul*, 77 F.3d 152, 155 (7th Cir. 1996) ("To say, as *Kimbell Foods* … do[es], that federal creditors presumptively have the same rights under state law as do private creditors is to say that they also have the same obligations and limitations").

Moreover, contrary to its position here, the FCC also argued in *Airadigm* that the scope of its security interest was defined not just by promissory notes and security agreements, but also by the agency's *regulations*. *See Airadigm*, 2008 WL 649704, at *10.[4]

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[4] As the Seventh Circuit summarized the FCC's argument:

> The FCC's second claim is that the bankruptcy court did not properly preserve the liens securing its claim in the licenses because it did not keep the FCC's due-on-sale rights . . . . The FCC's regulations provide that a licensee who obtained its licenses under the installment plan must pay back the full amount if it seeks to transfer the licenses . . . . 47 C.F.R. § 1.2111(c)(1). Because, in the FCC's estimation, the 2006 plan does

Thus, the FCC itself insisted in *Airadigm* that its roles as regulator and secured creditor are intertwined – *not* "separate and independent," Pet. App. 19a. The one consistent element in the FCC's position in *Airadigm*, *NextWave* and the present case is that the agency always switches back and forth between creditor and regulator roles – or even a combination of both – depending on whether the market is up or down. The FCC's disavowal of its secured creditor status in the present case can no more be reconciled with the agency's own arguments in *Airadigm* than with this Court's and the D.C. Circuit's decisions in *NextWave*.

4. The FCC's excursion into the merits, Opp. 12-17, also highlights fundamental errors inviting this Court's review. The FCC asserts that license cancellation is not a creditor remedy because it occurs pursuant to a regulation. Opp. 14. But that circular argument begs the question by presupposing the agency's regulatory and creditor roles are mutually exclusive. It also contradicts the

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> not preserve the [regulatory] due-on-sale provision, it does not "retain the liens."

Id. Ultimately, the Seventh Circuit rejected the FCC's argument because a due-on-sale provision (whether contractual or regulatory) is a "term of payment" that a bankruptcy court may alter, not an essential term of a lien that must be preserved in bankruptcy. *Id.* at *11. Nonetheless, the FCC's *regulatory* due-on-sale provision plainly defines the FCC's rights as *creditor*, even if (as the Seventh Circuit held) the bankruptcy court may modify those particular creditor rights. Thus, as the FCC's own arguments in *Airadigm* make clear, the dichotomy between the agency's roles as regulator and creditor (which the Ninth Circuit accepted below) is illusory.

unequivocal terms of the FCC's own security agreement (itself required by regulation, 47 C.F.R. § 1.2110(g)(3)), under which regulatory cancellation is *also* the FCC's primary remedy as creditor for default under the notes and security agreement. Pet. App. 88a. The regulatory dimension of cancellation is entirely consistent with its creditor aspect. *See NextWave*, 254 F.3d at 151; *Airadigm*, 2008 WL 649704 at *10 (recounting FCC's argument that its creditor remedies are defined in part by its regulations). Acting here like any other secured creditor, the FCC responded to a payment default by seizing its collateral, in this case through regulatory cancellation of the licenses.

Equally meritless is the FCC's suggestion (Opp. 16-17) that even if the regulatory cancellation here represents a disposition of collateral under the security agreement (which it does), federal common law incorporating U.C.C. Article 9 would not apply. As conceded in the FCC's own *Kennedy* opinion letter, under *Kimbell Foods* these security agreements are governed by federal common law that incorporates the U.C.C., unless specifically displaced by other federal law. *Leonard C. Kennedy, Esq.*, 11 F.C.C.R. 21572, 21578 (1996).[5] The FCC

[5] Contrary to the FCC's assertion, Opp. 16-17, this is consistent with the Seventh Circuit's holding in *Airadigm*, 2008 WL 649704 at *8-*9, that the Communications Act displaces state law that would otherwise allow a *private* judgment creditor to obtain a lien in FCC licenses. Federal law incorporating U.C.C. Article 9 still governs *other* aspects of the security arrangement – including the right to surplus proceeds – that do not conflict with specific federal enactments.

has never been able to point to any federal law that might displace Article 9 concerning entitlement to surplus proceeds from the FCC's cancellation and resale of license rights in response to nonpayment by a debtor-licensee. *See* Pet. App. 38a ("nothing in the Federal Communications Act (FCA) or FCC regulations governs this issue"). The best the FCC can do is point to conclusory statements in the *Kennedy* opinion letter itself – not in any federal statute or regulation. But as the Ninth Circuit recognized, that opinion letter plainly lacks the binding force of law. Pet. App. 9a-10a n.7; *see Christensen v. Harris County*, 529 U.S. 576 (2000).[6]

In tacit acknowledgment that its position conflicts with black-letter law governing secured transactions, the FCC tries to shift the discussion to easements or leaseholds, asserting that the law that applies to such interests would not give an easement- or lease-holder any right to surplus proceeds when the interest is cancelled. Opp. 16. But regardless of the rule under *other* bodies of law, the law of secured transactions that applies here *does* give a debtor like Magnacom a right to surplus proceeds resulting from the disposition of collateral.[7] Thus, while the FCC

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[6] The FCC's detour (Opp. 15) into whether the Trustee has any additional rights under the Bankruptcy Code is simply irrelevant. As the Ninth Circuit recognized, the applicable federal common law incorporating the U.C.C. is distinct from any claim under the Bankruptcy Code. Pet. 15-16.

[7] The easement and leasehold analogies are also inapt because though the United States regulates the airwaves, it does not "own" them. *See In re NextWave Personal Commc'ns, Inc.*, 200 F.3d 43, 52 (2d Cir. 1999).

suggests that the surplus would be a "windfall" to Magnacom's estate and its other creditors, Opp. 9, in the eyes of the law based on centuries of experience the equities are just the opposite: it would unjustly enrich a creditor like the FCC if it could keep more from the disposition of its collateral than the actual amount of the debt owed. In fact, the equities weigh so heavily in favor of a debtor like Magnacom in these circumstances that its right to surplus proceeds *cannot be waived*. Pet. 12, 32-33.

5. Finally, the FCC argues that this case is not certworthy because the agency has discontinued the specific secured-debt program under which Magnacom purchased its licenses. While the program may have ended, however, litigation concerning it continues to move through the lower courts. *See, e.g.*, *In re Urban Communicators PCS Ltd. P'ship*, 379 B.R. 232 (Bankr. S.D.N.Y. 2007).

More fundamentally, the question presented here is not limited to a single FCC program. As the FCC's former General Counsel has explained, this FCC program exemplifies the modern trend in which federal regulatory agencies become market participants in order to harness market forces for regulatory purposes. John A. Rogovin & Roger D. Citron, *Lessons from the NextWave Saga: The Federal Communications Commission, the Courts, and the Use of Market Forms to Perform Public Functions*, 57 Admin. L. Rev. 687, 693-96 (2005). As a result, "the distinction between 'regulatory' and 'private' in the characterization of government action has been blurred." *Id.* at 699; *see also id.* at 711-12 (noting that FCC acted as "both a regulator . . . and a

creditor due to the structure of its transaction with NextWave"). Thus, while "[a] narrow view of *NextWave* is that the case did no more than address the application of a single provision of the Bankruptcy Code," such a "view verges on myopia because *NextWave* implicated the fundamental question of the scope of the Commission's regulatory authority." *Id.* at 688; *see also id.* at 707-10 (recognizing a parallel to *United States v. Winstar Corp.*, 518 U.S. 839 (1996), in which the Court also addressed public-private regulatory hybrid in context of specific program that had been discontinued). And "although the agency may act in a dual capacity," courts often force hybrid agency actions into "an 'either-or' determination." *Id.* at 711.

This case presents that same fundamental issue of how to analyze an administrative agency's dual roles in this kind of hybrid program: does the agency exercise two "separate and independent" powers as regulator and creditor, as the Ninth Circuit held, Pet. App. 19a, or does it perform both roles at once, as the D.C. Circuit recognized, *NextWave*, 254 F.3d at 151. This issue is not limited to one FCC program. Indeed, every federal agency that extends credit subject to security interests does so in furtherance of a regulatory agenda and has an interest in using its regulatory powers to escape the obligations of ordinary secured creditors under *Kimbell Foods*. *See*, *e.g.*, *United States v. Walter Dunlap & Sons, Inc.*, 800 F.2d 1232, 1238-39 (3d Cir. 1986) (refusing to enforce agency's regulation imposing restrictions on proceeds of collateral that conflicted with state debtor-creditor law

incorporated as federal law). By emphasizing the regulatory dimension of the FCC's conduct while ignoring its creditor aspect, the Ninth Circuit's decision creates substantial uncertainty among private creditors who depend on the settled predictability of state law when entering into transactions involving federal agencies. *See Kimbell Foods*, 440 U.S. at 739. Particularly in light of the conflict with the decisions in *NextWave* and the FCC's own recent litigation position in *Airadigm*, this Court should review the decision below.

CONCLUSION

The Petition should be granted.

Respectfully submitted,

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