Viewpoint

One of a series of opinion columns by bankruptcy professionals

FCC Cross-Ownership Fog Impedes Media Restructurings

By Kenneth R. Yager II and Nicholas M. Miller

Turnaround professionals dealing with industries in fundamental decline ordinarily focus on a company's strengths and attempt to form strategic alliances to access new markets. For example, the Timken Company, which originally manufactured roller bearings for 19th century horse-drawn wagon wheels, adapted to secular changes in the wagon and carriage industry by applying its roller bearings to a much wider range of products. This allowed Timken to not only survive, but also develop into the Fortune 500 Company that it is today.

More recently, distressed media companies have argued that exploiting synergies among the broadcast, online and print media sectors may be one way of remaking their business models and ultimately allowing them to survive secular changes occurring in their industry.

But a major impediment to such media consolidation is the uncertainty regarding the Federal Communications Commission's rules limiting cross-ownership of newspapers and broadcast media - rules that were established 35 years ago and before the media industry made its dramatic transformation.

It's safe to say that the media industry has seen better times. In the past two years alone, more than 62 companies with radio, television, newspaper or magazine operations have filed for federal bankruptcy protection. Among the best known casualties are *Reader's Digest*, Air America, the Tribune Co., the Minneapolis *Star Tribune* and the *Philadelphia Inquirer*. Several venerable newspapers, such as the *Rocky Mountain News* and the *Seattle Post-Intelligencer*, have shut down print operations. Scores of other smaller market media companies have suffered the same fate. These bankruptcy filings and closures have wiped out billions of dollars in debt and equity holdings.

Turnaround experts note that the media industry's recent struggles are partly cyclical in nature. Advertising continues to comprise the vast majority of media revenues, and that source of revenue has declined sharply during this latest downturn, considered the worst since the Great Depression. Newspapers, for example, derive about 80% of their total revenue from print and online advertising, particularly from the retail, real estate and automotive industries - the very sectors hit hardest by the current recession.

Normally, such struggles would not be a source of undue concern for the media industry, which has a long history of overcoming cyclical downturns. Since World War II, the industry has not only survived 10 recessions, but also maintained impressive overall long-term growth and survived many "new media" intrusions. While the current recession is certainly painful, it is not necessarily, by itself, a cause for serious concern for the long-term health of the industry.

The real source of concern is secular change currently affecting the industry, most notably change related to content-delivery technologies and end-user expectations. Daily newspapers and television and radio broadcast outlets are no longer the only source for traditional hard news. Instead, the 24/7 cable news cycle and the Internet - increasingly accessed through BlackBerrys, iPhones and other portable devices - have become the norm. Content not immediately delivered becomes obsolete. Worse yet, end users increasingly expect content to be free.

According to industry pundits, 1993 was the peak subscription year for newspapers, and Netscape's web browser in 1994 changed news acquisition for the entire next generation of adults. With this backdrop, it's no wonder that industry experts worry about the long-term survival of traditional media.

FCC rules limiting cross-ownership between newspapers and broadcast media were established in 1975 when the typical city had a single daily newspaper and three major broadcast television stations. Those rules prohibited a single entity from owning both a newspaper and a broadcast radio or television station in the same market.

Since then, the FCC has failed to successfully address the rise of new forms of media and its effect on viewpoint diversity. In 2003, the FCC lifted the blanket ban on cross-ownership in favor of a pre-weighted "diversity index" requiring the FCC to consider all forms of media - both old and new, including the Internet - when evaluating the effect of a proposed consolidation on viewpoint diversity. Opponents challenged the new rule, and the 3rd U.S. Circuit Court of Appeals issued a remand order requiring the FCC to further explain the relative weighting assigned to the Internet in determining a market's media concentration.

In response to the 3rd Circuit's order, the FCC issued yet another set of new rules in 2008, this time scrapping the "diversity index" altogether in favor of a case-by-case approach requiring consideration of specified factors. Almost immediately, proponents and opponents of cross-ownership challenged the new rules. The effectiveness of the 2003 and 2008 rules were stayed pending resolution of the various lawsuits, all of which were later consolidated in the 3rd Circuit. Seven years later, cross-ownership rules still remain mired in a tangled mess of litigation and administrative rulemaking.

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From a restructuring perspective, this uncertainty is particularly unhelpful at a time when the media industry needs more flexibility to implement creative solutions to its financial problems. Often, the most logical and value-maximizing restructuring option for a distressed media entity would be to combine it with another broadcast or publishing company in the same market. Without clarity regarding FCC rules on cross-ownership, however, this type of restructuring option does not exist, increasing the number of failed media companies.

Fortunately, recent developments suggest that clarity soon may come from both the courts and the FCC. On the judicial front, the 3rd Circuit recently lifted the stay on the effectiveness of the 2008 rules and set a briefing schedule for the consolidated appeals. Thus, the case-by-case approach to cross-ownership adopted in 2008 is now effective, though still subject to reversal on the merits by the 3rd Circuit.

On the administrative front, the FCC recently commenced a new round of rulemaking, which may clarify cross-ownership rules later in 2010. Unfortunately, those clarifications may not arrive soon enough to help distressed media companies, which in the interim are unlikely to rely on the case-by-case approach because of the possibility of reversal by the 3rd Circuit.

Moreover, many observers expect the new 2010 rules to tighten cross-ownership restrictions, not loosen them, given the FCC's current board composition and known policy preferences. Thus, even if clarity is on the way, it actually may reduce rather than expand out-of-court restructuring options available to distressed media companies.

Until then, bankruptcy and restructuring professionals must continue to look for options other than consolidation of newspaper and broadcast media. And the media industry itself must hope that those options are enough to allow it to survive.

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Forum Health

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An Ardent subsidiary, AHS Newco 9 LLC, has offered to lead the bidding at auction with its $69.8 million offer. AHS Newco also has negotiated multi-year agreements with all of Forum Health's unions.

Forum Health's creditors, however, pointed out in court papers that the hospital operator is not a party to the changes Ardent negotiated to the collective-bargaining agreements. As a result, Forum Health doesn't have the authority to transfer the changes to any other potential buyer, including to those that would pay more for the assets if they could also obtain modified union contracts.

"It strains credulity to believe that any other potential buyer (including those who may wish to pay more for the assets) would submit a bid that did not contemplate CBA modifications," the creditors said.

The creditors also said that Ardent had seven months to negotiate the changes to the collective-bargaining agreements, but all other potential bidders would have to negotiate their own changes in an "extremely compressed timeframe." Forum Health is proposing an auction date of July 15.

The alternative for potential bidders is that they buy Forum Health's assets in hopes that the necessary changes to the collective-bargaining agreements are made after the sale.

"These hurdles will either deter parties from bidding altogether or require parties to effectively handicap their bids in order to hedge against the risk that they may not obtain union concessions necessary to successfully operate," the creditors said.

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