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Identifying and Resolving Telecom Law Issues in Acquisitions and Transactions

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For lawyers and the clients they serve, communications services are the lifeblood of the modern business. Today, communications issues will arise in virtually any (a) acquisition of a business or (b) commercial real estate transaction. They need to be identified early in the due diligence process and dealt with expeditiously. Otherwise, the issues may very well delay, or in an extreme case, derail a transaction.

In the United States, authorizations, licenses and permits for communications-related facilities and services ("Licenses") are issued at the federal level by the Federal Communications Commission (FCC).¹ At the state level, licenses are issued by state public utilities or public service commissions (PSCs). Licenses can cover services such as voice telephony services² or fleet dispatch radio.³ They can also cover specific facilities such as satellite uplink stations,⁴ microwave towers,⁵ or undersea cables.⁶ Providers of cable television services, moreover, are also required to obtain franchises from local jurisdictions -- usually a city or county.

A. Due Diligence In Telecom Issues

In any these transactions, counsel for the buyer must identify the seller's Licenses and communications-related contracts at the initial due diligence stage of an acquisition -- *whether or not the acquired firm is a telecommunications or cable company*. Early identification of Licenses is particularly crucial because (1) most of these Licenses cannot be transferred to an unaffiliated entity without the prior approval of the licensing agency, (2) obtaining that approval involves a lengthy public notice and comment period, and (3) as explained more fully in the Sidebar, the FCC is currently in the process of reconfiguring the Licenses that many businesses use to operate their internal radio systems, and there is a limited timetable during which the businesses must act to comply with the new rules.

Importantly, the due diligence involved is neither extensive nor expensive. In most cases, it involves obtaining a complete corporate organization chart, reviewing corporate records and

FCC licensing databases, and asking questions of a few key corporate employees. In fact, the most important step is simply recognizing the need to make the inquiries.

Obviously, there will be a focus on communications issues when the transaction involves a communications entity, such as a cable television system, or a firm inherently dependent on communications, such as a webhosting firm, a call center or a travel agency. But counsel needs to keep in mind that it is not just communications companies that hold Licenses.

B. Issues Faced By Non-Telecom Companies Holding Licenses

Three recent transactions in which one of the co-authors was involved vividly illustrate this fact. In the first, the seller of a brickmaking facility had leased space for a cellular telephone antenna on a particularly tall smokestack, effectively turning the smokestack into an FCC-licensed cellular tower. Because the issue was identified early, it was easily resolved.

In the second transaction, a client was buying two small specialty plastics manufacturing plants from a large national firm. The entity owning the manufacturing plants held microwave and very small aperture satellite (VSAT) licenses for facilities that linked the plants to the corporation's computer network -- many multi-location businesses, ranging from Wal-Mart to banks, hold such licenses. In the third, a client was buying a thriving regional bakery and the associated fleet of trucks that delivered the bakery's goods to retail outlets. The bakery held a number of business radio licenses that enabled real-time private communications between the plant and delivery truck drivers. *In the second and third cases, neither the buyer nor its corporate counsel realized until the closing was approaching that the firm being purchased held Licenses issued by the FCC.* In both transactions, communications counsel was immediately brought in once the Licenses were discovered. Unfortunately, the need to obtain FCC approval for transfer of the Licenses on an expedited basis substantially increased the cost of obtaining the approvals, and in one case the late discovery of the License forced a costly postponement of the closing date.

C. Contractual Issues Faced By Non-Telecom Companies

Some communications issues go directly to the calculation of the purchase price. For example, in transactions involving buildings with commercial tenants -- whether a stand-alone real estate transaction or part of a corporate acquisition -- a buyer should determine whether the building owner has entered into an exclusive arrangement with a communications carrier to provide communications services to the building and all the tenants. If so, the buyer may want to discount or ignore the cash flow from payments by the carrier under contract in calculating the purchase price for the building. The payments would be at great risk because such contracts are not enforceable. The FCC has held that competing carriers cannot be prevented from gaining access to a commercial building, and it has prohibited carriers from entering into exclusive contracts with commercial building owners.⁷

Other communications issues may alter the economics of a deal after it has closed. At a minimum, buyers must carefully review potentially applicable contracts for voice and data services, including contracts for mobile, internet access, ATM,⁸ frame relay⁹ and WANs.¹⁰ For example, in the plastics transaction discussed above, certain communications services were provided under the selling firm's nationwide "take or pay" contract¹¹ that could arguably have continued to apply to the plants after the acquisition, which would have resulted in duplicative communications expenses for the buyer. Once the issue was identified, the seller agreed to be responsible for resolving it with the carrier and to indemnify the buyer for any expenses arising from that contract. Corresponding amendments to the asset purchase agreement had to be made.

In other situations, where ongoing savings from consolidation of communications services are part of the buyer's price calculation, review by communications counsel will be necessary to determine whether budgeted savings can in fact be achieved. This typically involves analysis of the specific language of three types of clauses commonly found in communications services contracts: (a) the minimum revenue commitment clause, (b) the substitution of services clause, and (c) the business downturn/sale of the business clause. The interplay of these three clauses can be crucial for data intensive industries, such as banking, finance and information technology.

Conclusion

In the 21st century, as communications services become increasingly critical to business in the United States and around the world, communications-related issues will move to the forefront in commercial real estate transactions and business acquisitions. And they affect virtually all businesses. Every business lawyer -- from antitrust and IP to tax lawyers -- must be aware of such issues and must perform due diligence in the early stages of the deal to effectively identify and resolve them. Failure to do so is not only expensive, but may delay or, in some cases, even derail the transaction altogether.

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ENDNOTES

1. 47 U.S.C. § 151 (2005). See also 47 C.F.R. § 2.102 (assignment by FCC and use of radio frequencies).
2. *Telephony* refers to the processes of transmitting and receiving sound -- usually speech, tones which represent digits for signaling, and graphics.
3. A *fleet dispatch radio* allows work crews to communicate, often through a main dispatcher who can relay messages to the entire group or individuals.
4. A *satellite uplink station* is a radio link between a station on Earth and a satellite, used for transmitting information globally.
5. *Microwave towers* can transmit and receive communications through microwaves, which, loosely, are signals transmitted through the air rather than through cables or wires.
6. *Undersea cables* transmit information and are placed at strategic locations underneath oceans and seas and make much of the world's international communications traffic possible.
7. If a competing carrier were to demand access to the building, the new owner would have to negotiate to grant the access and the carrier with the exclusivity would probably stop making the payments.
8. *ATM* is short for Asynchronous Transfer Mode; a technology used for transferring packets of information in a network.
9. *Frame relay*, like ATM, is a manner in which packets of information are transferred in a network.
10. A *WAN* is a wide-area network; a group of computers connected together, often over telephone lines, over a large geographic area.
11. In telecom law and other areas, a *take or pay contract* is an agreement between a buyer and seller in which the buyer will still pay some amount even if the product or service is not provided.