

# Some notes from the spectacular Tribune Sinclair lawsuit \$SBGI \$TRCO

I've been looking at the local broadcasters (Nexstar, Tribune, Sinclair, etc.) recently (no position in any of them currently) due to a combination of curiosity, cheapness, and interest in the sector given overlap with a lot of my cable / telecom investments. I might have a (much) longer article on them at some point on the big question that looms over them (and basically the entire legacy cable bundle): what happens if one of the major networks loses their NFL package when they're up for renegotiation in the next year or two? Doesn't that throw everything related to that specific network (the network, all of their contracts with cable companies and local broadcasters, all of the local broadcasters' contracts, etc.) into complete chaos?

Anyway, that's a question for another day. As part of the broadcast sector research, I've been reading [Tribune's lawsuit against Sinclair](#) for "[repeatedly and willfully](#)" breaching "[its contractual obligations in spectacular fashion](#)" in , and the suit is one hell of a read (here's [the complaint](#), and [here are the exhibits](#)). I'll caveat everything I'm about to say by noting this is all my opinion and I am by no means an expert in this area (I'm simply an investor with an interest in the sector; I'm not a lawyer, I haven't seen Sinclair's response to Tribune yet, I'm no expert on FCC and DOJ regulatory issues, and I haven't completely finished researching Sinclair yet), but my takeaway from reading Tribune complaint is pretty simple: Sinclair is completely uninvestable. And I don't just mean their equity is uninvestable at today's prices but would be interesting a bit lower; with all of the issues facing them, I wouldn't want to touch a single piece of Sinclair's capital structure unless I was getting truly distressed pricing. Why do I think Sinclair's whole cap structure is uninvestable? It's not just that they're likely to lose the Tribune complaint (though they are almost certainly losing that); it's that Sinclair seemed to damage their reputations at the regulatory agencies (FCC and DOJ) so badly that I don't see how any seller could take Sinclair seriously as a buyer for years (Tribune accuses Sinclair of engaging in "belligerent" negotiations with both the FCC and DOJ and says [Sinclair "'fought, threatened, insulted, and misled regulators"](#) and notes Sinclair completely disregarded "repeated warnings from both Tribune and the regulators" that their approach would cause the deal to die). On the extreme downside, there's a non-zero chance that the FCC uses what happened in the Tribune and rules that Sinclair doesn't meet their "[character policy](#)", which would let the FCC strip Sinclair's licenses and (I believe) sell them without any of the proceeds going to Sinclair. That's probably a bit extreme, but Sinclair messed with the regulators in a way that has become so public (and could become even more public as Tribune's lawsuit

makes its way through court) that I would guess regulators try to take their pound of flesh from Sinclair for years to come.

And if that type of regulatory tail risk wasn't enough, you also have to worry about the fact Sinclair's (alleged) self-dealing and lying doesn't just extend to trying to pull one over the regulators; it also looks like they have a history of selling company assets for far below market value to related and/or controlled parties. Here's some of the examples the FCC pulls in (they're all listed in exhibit B of the suit):

- As part of their divestiture package, Sinclair tries to sell WGN-TV Chicago, one of Tribune's "crown jewels", for \$60m. The FCC notes that's "far below market value" and the most recent comp for that station had gone for \$425m ("over seven times the sales price") in 2002.
- Sinclair allowed a buyer of some other divestitures "to obtain the stations at a small fraction of their value"
- For their Dallas and Houston divestitures, Sinclair sells both stations to a related party for \$60m total while guaranteeing \$53.6m of debt related to the transaction (the FCC notes these sales terms were "atypically favorable to the buyers," which seems a bit of an understatement). The FCC notes it appears these were sold "far below the expected market price"; the combined price of \$60m for the two stations (which are located in the 5<sup>th</sup> and 7<sup>th</sup> largest markets in the nation) was less than the \$65m price Meredith agreed to pay for one station in the 21<sup>st</sup> largest market.

Put it all together, and you get a company that can no longer participate in consolidation (either because regulators won't let them or sellers simply can't trust them, and lot of value for broadcasters is created through M&A), that could be facing existential risk from their regulators, that will likely lose to Tribune in court and need to pay a huge judgement, and where management doesn't really seem to care about minority shareholders (I don't know Sinclair super well, but based [on their must carries](#) and the complaint I don't think it's crazy to suggest they're focused on maximizing political reach) but has entrenched themselves in control with super voting shares. How much of a discount would you need on the equity or debt to invest in the face of that type of tail risk? I'm not sure, but (for me) it's nowhere around today's levels (which seem to factor in a small loss in the Tribune lawsuit and nothing else; why buy Sinclair and face all that regulatory risk when you could buy any of the other broadcasters for roughly the same multiple once

you adjust for likely damages in the Tribune case?).

Maybe everything above seems a bit of hyperbole to you (in particular, a lot of Sinclair's self-dealing does seem to keep some profits at the Sinclair level versus funneling it out to related parties), so below I present the most shocking pulls from the Tribune complaint (and I assure you there were more but they tended to be a bit more technical or drier (for example, Tribune accusing Sinclair of using a contingent trust structure that "stood virtually no chance of approval" and "had the inevitable effect of necessitating the attempted use of a Rube Goldberg type divestiture trust structure" is both hilarious and holds a special place in my heart for its [throwback to the Time Warner trial](#)); I tried to limit myself to just the real eye catchers). Read through them and I think you'll agree with me that Sinclair would need to price in some serious distress to be worth the huge tail risks here (or at least you'll get a good laugh!).

- The complaint starts with a broad overview of Sinclair's interactions with the DOJ; I'll drill into some of the points a bit more later but the broad overview: the DoJ tells Sinclair that if Sinclair agrees to sell the stations in the ten markets with overlap (i.e. Sinclair and Tribune both own a station), the deal will be approved (a direct DoJ quote is "we would be done"). Sinclair responds by (and I'm just going to quote the whole thing from the suit, because it's incredible) "antagonizing DOJ officials, including by accusing the Antitrust AG - the highest ranking official in that division of 'completely misunderstanding' the broadcast industry and being 'more regulatory' than any recent predecessor. Sinclair invited litigation over station divestitures, including summarizing its position to DOJ in two words: 'sue me.' Indeed, Sinclair went so far as to threaten to file its own lawsuit *against* the DOJ."
- It's the regulatory equivalent of [Bachman putting his balls on a VC's table](#), except if instead of getting \$15m Bachman had invited the wrath of his regulators for the rest of time.
- Sinclair proposes selling WGN-TV to a corporation that "had been controlled by the estate of Smith's (the Executive Chairman of Sinclair) late mother until January 2018".

- Tribune notes that Sinclair didn't just belittle and confront the DOJ staff "without basis"; Sinclair actually belittled / confronted "AAG Delrahim" himself.
  - Belittling Delrahim for following pretty vanilla station overlap rules seems pretty crazy; if you're going to belittle him for anything, you've got to belittle him for [continuing to fight the AT&T / Time Warner](#) battle after an "embarrassing defeat" (or maybe just belittle him for bringing such a crazy case in the first place).
  - Despite belittling the DOJ and Delrahim himself, the DOJ offers a "clear path" towards regulatory approval, but Sinclair "squandered this golden opportunity" and soon threatens the DOJ with litigation (a breach of their merger agreement).
- Tribune later says Sinclair's excuse for not meeting their regulatory burden is "patently false".
- Sinclair sends a letter to the top brass of the DOJ and compares their "leadership unfavorably with that of the FCC- an approach that was as unhelpful as it is now ironic".
  - The Sinclair letter is legit insane. AT&T and Time Warner were less hostile to the DOJ in their court case against the DOJ than Sinclair is in this letter. I won't quote the whole thing here (part of it is included on page 33 of the complaint and the whole thing is in exhibit E), but it includes Sinclair accusing the DOJ of being "unwilling to recognize how completely the world has changed." They of course criticize the DoJ's understanding of the broadcasting industry, and they go on to question how the DOJ is taking depositions. The letter ends with some other "inflammatory assertions" (Tribune's words).
  - In a follow up meeting, Sinclair includes a divestiture offer that was a "manipulation" the DOJ rejected as "disingenuous".
- Next comes the infamous (in my mind) meeting where Sinclair tells the DOJ "sue me". However, they don't

stop there; they also tell Tribune that Tribune will need to sue Sinclair if they want Sinclair to meet their divestiture obligations.

- To threaten both the government and your merger partner in one meeting is pretty spectacular work.
- In future calls, Sinclair becomes both “bullying and insulting in tone” with the DOJ, going so far as accusing the DOJ and Delrahim of “completely misunderstanding the industry” and being “more regulatory than anyone before you, under any other president for 21 years.”
- Soon Sinclair resorts to lying to the regulators; on February 20, Sinclair lies to the FCC about the stations the DOJ will let them keep as part of their divestiture package.
- Tribune later accuses Sinclair of structuring their divestitures in “the most self-serving way” by selling to related parties who would wouldn’t mind “kicking back the preserved profits to Sinclair”. The proposal is “so provocative that FCC staff refused even to put” the proposal out for public comment.
  - If you go to exhibit B, you can the full FCC note on the subject; it includes a FCC Commissioner calling the sales a “sham intended to circumvent the local and national television multiple ownership rules.” Always a good thing when one of your regulators notes that your plan to comply with their rules is a sham and “egregious”.
  - Later the commissioner accuses Sinclair of engaging in “misrepresentation and/or lack of candor”; again, always good for a company when your regulator outright thinks you’re a liar!

The whole thing is a spectacular read; I’d encourage you to take the time to read it.