

In the Supreme Court of Ohio

DirecTV, Inc., and EchoStar
Satellite L.L.C.,

Plaintiffs-Appellants,

v.

Richard Levin, Tax
Commissioner of Ohio,

Defendant-Appellee.

09-0627

On Appeal from the Court of
Appeals, Tenth Appellate District

Court of Appeals
Case No. 08AP-32

BRIEF OF *AMICI CURIAE* PUBLIC KNOWLEDGE,
CONSUMER FEDERATION OF AMERICA, MEDIA ACCESS PROJECT, AND U.S. PIRG
IN SUPPORT OF JURISDICTION

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INTEREST OF THE *AMICI*

Public Knowledge, Consumer Federation of America, Media Access Project, and U.S. PIRG respectfully submit this brief in support of the petition for review by the Supreme Court of Ohio.

Public Knowledge is a Washington, D.C. based not-for-profit public interest advocacy and research organization. It is dedicated to protecting consumers' rights and the core democratic principles of openness, public access, and the capacity to innovate and compete in the digital age. Public Knowledge seeks to guard these cultural values at all layers of our communications systems through legislative, administrative, legal, and grass-roots efforts.

Consumer Federation of America is an advocacy, research, education, and service organization which works to advance pro-consumer policy on a variety of issues before Congress, the White House, federal and state regulatory agencies, state legislatures, and the courts. In addition to its policy efforts, Consumer Federation of America conducts research, educates the public and policymakers, and supports other like-minded organizations on consumer issues.

Media Access Project is a thirty-seven year-old non-profit public interest law firm which promotes the public's right to receive information. Its clients include civil rights, civil liberties, consumer and religious groups concerned about the right to speak and to be heard in the electronic mass media.

U.S. PIRG, the federation of state Public Interest Research Groups (PIRGs), takes on powerful interests on behalf of the American public, working to win concrete results for our health and our well-being. With a strong network of researchers, advocates, organizers and students in state capitols across the country, U.S. PIRGs stand up to special interests on issues

where powerful special interests stand in the way of reform, like product safety, identity theft, political corruption, prescription drugs, and voting rights.

The decision below has broad implications for consumer choice and costs as well as for the diversity of voices in the video services which are piped daily into over 3 million Ohio homes. The Court of Appeals has provided a recipe for state legislatures to favor in-state interests at the expense of interstate commerce. If these schemes, designed to create an anticompetitive market, are permitted to continue in the face of contrary Constitutional law, the cost of favoring some Multichannel Video Program Distributors (“MVPD”) over others will be paid for by consumers, speakers, and innovators. Simply put, sales taxes that discriminate among MVPDs based on the location of the equipment used to distribute programming limits competition and increases prices. *Amici curiae* uniquely represent the interests of consumers in a proceeding which is otherwise about the interest of states versus the interest of certain video providers.

None of *amici curiae* are affiliated with any cable company, Direct Broadcast Satellite (“DBS”) provider, other MVPD, or party to this action.¹

SUMMARY OF ARGUMENT

Tax schemes such as the one at issue in this case raise issues of great public and general interest because they harm the competition which is critical to ensuring that MVPD consumers receive the best service and have access to the greatest diversity of voices at the lowest price.

Competition in the MPVD market benefits consumers in three broad ways. First, competition in the MVPD market disciplines prices across providers, lowering costs for *all* subscribers to MVPD services and increasing the availability of services nationwide. Second,

¹ *Amici* would also like to acknowledge the assistance of Michael Weinberg, George Washington University Law School, in the preparation of this brief.

competition translates to diversity of voices heard by the vast majority of Ohio households who subscribe to multichannel services. Third, competition increases quality of service to multichannel customers. DBS-based competition in particular has a demonstrated track record of encouraging innovation in the market, providing consumers with advanced services including better picture quality, music offerings, and Internet and telephone services. Singling out innovative distribution technologies for discriminatory taxation discourages service improvement and encourages providers to freeze existing levels of service. Finally, these benefits are felt even more strongly by rural customers, who may have no locally based MVPD option at all.

Congress and the FCC have repeatedly demonstrated their commitment to achieving consumer benefits through competition in the MVPD market. By leveling the playing field, Congress has sought to stop runaway cable pricing and encourage innovation. To some extent, it has succeeded. But to the extent that MVPD prices still outpace inflation, the problem can be partially attributed to the discriminatory treatment of cable's primary competitor in a market where consumers, when faced with higher prices, are very likely to switch providers or leave the market entirely.

Finally, the issues raised by the Court of Appeals' decision apply not only to current MVPD competitors, but to future entrants as well. Creating an anticompetitive market by favoring some MVPD distribution technologies over others will harm consumers by restricting competition in existing video services and reducing the incentive to create new services which have not yet been imagined. We ask that this court review the decision of the Court of Appeals in order to determine that Ohio cannot engage in discriminatory taxation against some types of MVPDs.

THIS CASE INVOLVES MATTERS OF GREAT PUBLIC AND GENERAL INTEREST

In general, if any branch of trade, or any division of labour, be advantageous to the public, the freer and more general the competition, it will always be more.
Adam Smith, *The Wealth of Nations*, Book II, Chapter II (1776).

It is now axiomatic that competition is beneficial to consumers, both because it increases choice and because it lowers prices.² When a state acts to unconstitutionally disfavor out-of-state DBS interests in favor of in-state land-based MVPD interests, it hampers this critical competition and hurts all Ohio MVPD customers – a group that comprises over 85% of the Ohio public – in three major ways.

I. Ohio's Discriminatory Tax Harms Critical DBS-Based Competition in the MVPD Market

As Congress has long recognized, the pro-speech and pro-consumer effects of DBS-based competition are critical to the MVPD market: “There is a substantial governmental and First Amendment interest in promoting a diversity of views provided through multiple technology media,” and “[w]ithout the presence of another multichannel video programming distributor, a cable system faces no local competition. The result is undue market power for the cable operator as compared to that of consumers and video programmers.” Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, §§ 2(a)(2), 2(a)(6), 106 Stat. 1460, 1460 (1992) (codified at 47 U.S.C. § 521 note) [hereinafter 1992 Cable Act].

A. Congress Intended DBS to Provide Meaningful Competition in the MVPD Market

Congress has long been concerned with cable companies abusing their MVPD monopolies. *See, e.g.* 1992 Cable Act. With the large initial investment required to construct a cable network, cable has often been described as a natural monopoly. Although there have been

² For a more modern, in-depth explanation of the consumer benefits of competition, *see* F. M. Scherer & David Ross, *Industrial Market Structure and Economic Performance* (Houghton Mifflin Co. 1990).

attempts to diversify MVPD offerings by encouraging cable “overbuilders” (companies that construct a second cable network in communities with existing cable networks), these services have experienced problems reaching financial stability and economies of scale. *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video, 12th Annual Report* at 89-90, F.C.C. 06-11 (Feb. 2006) [hereinafter *12th Annual Report*]. Unlike overbuilders, who must construct large networks in every market before they can begin to compete, DBS services can quickly and easily distribute equipment to begin competing in a given market. This ease of entry into new markets provides a much-needed check on cable's monopoly power. *Id.* at 7.

B. A Discriminatory Tax Has a Major Impact on the Effectiveness of DBS Competition for Ohio Consumers

Consumers in the MVPD market are price-sensitive, meaning that small increases in the price of one provider will produce comparatively large shifts of consumers away from that provider, often to competitors. As a result, differential taxation will directly impact competition and harm all of the goals discussed below.

In summarizing eight studies of price elasticity in the MVPD market, two Brookings Institution fellows reported that “[t]he studies . . . all conclude that the own-price elasticity of demand for basic cable television service is price elastic. That is, a one percent decrease in cable price will induce more than a one percent increase in subscribers.” Robert W. Crandall & Robert Litan, *The Benefits of New Wireline Video Competition for Consumers and Local Government Finances* at 7 (2006), available at http://www.criterioneconomics.com/docs/TELCO_MVPD_Entry_Cable_Franchise_FINAL.pdf. Individually, the studies showed that such a 1% price change would change demand between 1.5% and 5.9%. *Id.* at 7.

These conclusions were further illustrated in a study on the Ohio MVPD market by Professor Yoram Wind. *See* Affidavit of Yoram Wind. Professor Wind concluded that over 32% of Ohio television households consider price to be an important factor when choosing television services. *Id.* at ¶ 14. Professor Wind's finding that 18% of Ohioans had their television services purchasing choices impacted by the tax in question is consistent with this high level of price awareness. *Id.* at ¶ 13. These households included cable customers who may have switched to DBS, antenna users who may have switched to DBS, DBS users who may not have left DBS for cable, and DBS users who may have purchased additional services from their DBS provider. *Id.*

These studies suggest that the type of cost changes imposed on DBS by the Ohio tax is likely to produce a drastic effect on competition. This directly impacts as much as 18% of Ohio's population and produces significant competitive harm, in turn increasing overall prices paid and reducing quality of service and the diversity of voices received by all Ohioans.

C. Rural Consumers Gain Additional Benefit from DBS Availability

More than 22% of Ohioans live in rural areas. Center for Family and Demographic Research, *Ohio Population News: Ohio's Rural Population* (Aug. 2004) available at <http://www.bgsu.edu/downloads/cas/file36245.pdf>. In addition to broadly competing with cable, DBS has a much higher adoption rate in rural areas. No. GAO-05-257, *Direct Broadcast Satellite Subscribership Has Grown Rapidly, but Varies Across Different Types of Markets* at 2 (Apr. 2005) [hereinafter *GAO Report*], available at <http://gao.gov/>. In areas where no cable service is available at all (which are often rural), DBS adoption rates are 53% higher. *Id.* at 2. This means that for consumers in such regions - where DBS is always available—discriminatory tax schemes will directly translate to an increase in consumer costs, driving a significant fraction of consumers out of the market altogether and producing higher prices for the rest. Further, any

harm to DBS in markets that have cable as well will visited more powerfully on rural customers, who do not have the benefit of a state-preferred option available.

II. Harm to DBS-Based Competition in the MVPD Market Results in Harm to Ohio Consumers

The benefits of competition in the MVPD market are realized by consumers market in three ways: First, competition between MVPDs reins in prices for all MVPDs. Second, it encourages MVPDs to diversity their offerings, resulting in a broader diversity of speech being available to consumers. Finally, competition drives both the creation of new, innovative MVPD offerings and an increase in quality of existing services. When Ohio's tax schemes harm competition from DBS, they also hurt Ohio consumers in all three areas.

A. Harm to MVPD Competition Results in Economic Harm to All Ohio MVPD Customers

Congress intended for DBS entry to provide meaningful price constraints in an otherwise monopolistic MVPD market. *See*, 1992 Cable Act § 19, 106 Stat. 1494. It has been partially successful, although current levels of competition have not been enough to completely discipline pricing. In its most recent report on competition in the video programming market, the FCC reported that despite technological improvements in video delivery, prices in the MVPD market continue to outpace the general level of inflation. Federal Communications Commission, *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video, 13th Annual Report* at 45, F.C.C. 07-206 (Jan. 2009) [hereinafter *13th Annual Report*].

Competition form DBS, however, *has* had the effect of constraining the price increases from incumbent providers, preventing them from rising even higher than they have to date. One study concluded that without DBS's entry into the market, cable prices would be 15% higher. Austan Goolsbee & Amil Petrin, *The Consumer Gains from Direct Broadcast Satellites and the Competition With Cable TV*, 72 *Econometrica* 351, 373 (2004). Especially given the price

sensitivity of MVPD customers, differential treatment of DBS and cable services in Ohio and other states could account for DBS's failure to fully control cable price increases despite its positive effect on other areas, including network availability, picture quality, and overall innovation.

In the same way that competition lowers prices for consumers, reduced competition raises them. If allowed to proceed unchecked, discriminatory taxing will raise prices not just for DBS users, but for *all* MVPD subscribers. This results not just in DBS customers paying higher prices (as is the case with all taxes), but in increased prices for services used and paid for by over 85% of Ohioans. *See* Affidavit of Yoram Wind ¶ 36.

B. Harm to MVPD Competition Reduces the Diversity of Voices Critical to a Democratic Society

As Congress has recognized, there is a "substantial . . . First Amendment interest in promoting a diversity of views provided through multiple technology media." *1992 Cable Act* § 2(a)(6). The Supreme Court of the United States has also recognized this Constitutional interest: "[A]ssuring that the public has access to a multiplicity of information sources is a governmental purpose of the highest order, for it promotes values central to the First Amendment." *Turner Broad. Sys. v. F.C.C.*, 512 U.S. 622 (1994). The FCC, too, has echoed the Supreme Court's observation that "[i]t has long been a basic tenet of national communications policy that 'the widest possible dissemination of information from diverse and antagonistic sources is essential to the welfare of the public.'" *In re Comcast Corp.*, 17 F.C.C.R. 23246, ¶ 27 (2002) (quoting *Turner Broad. Sys. v. F.C.C.*, 512 U.S. 622, 663 (1994)).

As of June 2006, there were approximately 95.8 million households in the United States that subscribed to an MVPD service. *13th Annual Report* at 8. According to the 2000 census, there are roughly 105 million households in the United States. *See USA Quickfacts*, United

States Census Bureau, *available at* <http://quickfacts.census.gov/qfd/states/00000.html>. And for the over 90% of households which subscribed to an MVPD service in 2004 and 2005, the average one tuned into television for over eight hours per day. *12th Annual Report* at 3.

In Ohio today, the delivery of video services to homes is much more than an entertainment business. It is a primary speech outlet—one through which Ohio households view over 9.5 billion hours of television-based speech per year. DBS has already made progress in promoting consumer choice and diversifying voices on this communications channel. In 2006, the FCC’s annual report on competition in the MVPD market stated that “[c]ompetition in the delivery of video programming services has provided consumers with increased choice, In particular, the effect of DBS competition has resulted in the addition of networks to cable operators’ channel line ups, . . .” *12th Annual Report* at 4. Further, DBS’s nationwide structure allows it to provide a wider variety of options than local cable franchises can. For instance, while foreign-language programming may not be economically viable in a given cable market, DBS can aggregate the demand for it nationwide and offer it to consumers in every market across the United States.

When a state grants some MVPDs preferential tax treatment, it not only raises prices for consumers, but reduces the diversity of voices and speech venues available to all Ohioans.

C. Harm to MVPD Competition Will Reduce Service Improvements Delivered to Consumers

In addition to delivering more diverse voices and lowering prices, the FCC noted that MVPD competition provided consumers with “better picture quality[] and greater technological innovation.” *12th Annual Report* at 4. The 2006 report indicates that consumers continue to receive these benefits. *See 13th Annual Report* at 4. Specifically, cable operators have made investments which enable “more channels of basic and digital cable services, premium movie

services, pay-per-view service, high-definition service, high-speed Internet access services, CD-quality music, cable telephony, and more personalized programming options.” *12th Annual Report* at 22.

The FCC attributes these new services in large part to competition from DBS; and in response to cable’s new services, DBS providers have expanded their own offerings: “Cable operators have responded to the growth of DBS and its competitive service offerings by, among other things, expanding their channel line ups and bundling video service with other service offerings, such as cable modem service or telephone service. . . . These competitive efforts are matched by DBS operators’ offering of local broadcast channels, additional sports and international programming, and advanced set-top boxes with digital video recorder (DVR) capabilities.” *12th Annual Report* at 4. This continual upgrading of services is emblematic of the benefits of competition.

The Government Accountability Office also reports that DBS penetration is 20% higher in places where cable is not offering these advanced services, suggesting that DBS’s presence forces cable to offer customers improved services in order to compete. *GAO Report* at 9. Taxes that disproportionately burden DBS to the benefit of cable will allow incumbents to slow or cease these innovations, as they will unnecessary for cable to compete in the marketplace.

PROPOSITIONS OF LAW

Amici Public Knowledge, Consumer Federation, Media Access Project, and U.S. PIRG adopt the propositions of law proposed by plaintiff-appellants.

CONCLUSION

For these reasons, this is a case of great public and general interest. *Amici* therefore request that the Court accept jurisdiction of this appeal and review the judgment of the Court of Appeals.

Respectfully Submitted,



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Certificate of Service

I certify that a copy of this Memorandum in Support of Jurisdiction was sent by ordinary U.S. mail to counsel listed below on April 6, 2009.

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