ORIGINAL

No. 2009-0627

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.

ON APPEAL FROM THE FRANKLIN COUNTY COURT OF APPEALS, TENTH APPELLATE DISTRICT, CASE NO. 08-AP-32

BRIEF OF AMICUS CURIAE STATES OF NORTH CAROLINA, UTAH, DELAWARE, FLORIDA, ILLINOIS, KANSAS, KENTUCKY, MARYLAND, MICHIGAN, MISSISSIPPI, MISSOURI, RHODE ISLAND, TENNESSEE, VIRGINIA AND WEST VIRGINIA IN SUPPORT OF DEFENDANT-APPELLEE

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I. INTEREST OF *AMICUS CURIAE*

The Amici States write in support of Richard Levin, the Ohio Tax Commissioner, and urge the Court to affirm the Court of Appeals' holding that Ohio's sales tax on satellite television service does not impermissibly discriminate against interstate commerce in violation of the United States Constitution. The Amici States have a keen interest in ensuring the consistent and rational development of commerce clause jurisprudence, including recognition of the fundamental principle that a taxpayer challenging the constitutionality of a tax statute on commerce clause grounds bears a high burden of proving that the tax in question actually discriminates against interstate commerce. To establish discrimination in practical effect – the only challenge preserved by appellants – the satellite companies must establish by clear and unambiguous evidence that the tax differentiates between local and out-of-state interests and the distinction is based on geographic location rather than differences in modes of operation. They must present evidence of substantial distinctions and real injuries. If a taxpayer can successfully attack a taxation statute without the requisite showing of actual – rather than hypothetical or speculative – discrimination, state legislatures will be stripped of the traditional deference that they have been afforded in crafting taxation statutes. As every other appellate court to consider the question has concluded, appellants simply cannot shoulder their heavy burden.

II. ARGUMENT

PROPOSITION OF LAW

APPELLANTS HAVE NOT AND CANNOT DEMONSTRATE THAT THE OHIO STATUTE UNCONSTITUTIONALLY DISCRIMINATES AGAINST INTERSTATE COMMERCE

For the reasons set forth in Ohio's brief, the Amici States urge this Court to affirm the decision of the Court of Appeals. Rather than reiterate each of Ohio's arguments, the Amici States write to emphasize several points of critical interest to the States.

Courts have long recognized that state legislatures must be free to devise tax systems that meet the myriad needs of their citizens without unnecessary interference from the judiciary. See, e.g., *American Trucking Ass'n, Inc. v. Michigan Pub. Serv. Comm'n* (2005), 545 U.S. 429, 434 ("*American Trucking II*") (Constitution does not unduly curtail States' power to lay taxes to support state government) (citing *McGoldrick v. Berwind-White Coal Mining Co.* (1940), 309 U.S. 33, 48). Mindful of this policy of judicial restraint, this Court has recognized that only in extraordinary circumstances are state taxing statutes declared unconstitutional:

> A court's power to invalidate a statute is a power to be exercised only with great caution and in the clearest of cases. Laws are entitled to a strong presumption of constitutionality and the party challenging the constitutionality of a law bears the burden of proving that the law is unconstitutional beyond a reasonable doubt.

Columbia Gas Transmission Corp. v. Levin, 117 Ohio St.3d 122, 2008-Ohio-511, 882 N.E.2d 400, 410, at ¶41 (internal quotations and citations omitted), cert. denied (2009) 129 S. Ct. 896. Here, the appellants simply cannot shoulder their burden of proving that Ohio's tax is unconstitutional.

"To determine whether a law violates th[e] * * * 'dormant' aspect of the Commerce Clause, [this Court must] first ask whether [the Ohio tax law] discriminates * * * against interstate commerce." *United Haulers Ass'n v. Oneida-Herkimer Solid Waste Mgmt. Auth.* (2007), 550 U.S. 330, 338. "In this context, 'discrimination' simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." Id.

To establish discrimination in practical effect, appellants must demonstrate beyond a reasonable doubt that the sales tax "favors in-state business over out-of-state business for no other reason than the location of its business." *American Trucking Ass'n v. Scheiner* (1987), 483 U.S. 266, 286 ("*American Trucking I*"). As the United States Supreme Court instructed in *General Motors Corp. v. Tracy* (1997), 519 U.S. 278, 299, "[c]onceptually, of course, any notion of discrimination assumes a comparison of substantially similar entities." Finally, only actual, rather than hypothetical, discrimination gives rise to a commerce clause violation. *Associated Indus. of Mo. v. Lohman* (1994), 511 U.S. 641, 654. Appellants have not sustained their burden with respect to any of the foregoing requirements.

A. Appellants' Novel "Relative Presence" Test Sharply Deviates from Supreme Court Precedent and Is Dangerously Unworkable

Appellants simply cannot meet their burden to show that an in-state economic interest exists in this case. "[N]either satellite companies nor cable companies are properly characterized as an in-state or out-of-state economic interest." *DirecTV, Inc. v. State* (2006), 178 N.C.App. 659, 664, 632 S.E.2d 543, 548. "[C]able companies are no more 'local' in nature than are satellite companies. Indeed, * * * both businesses are interstate in nature, as they both utilize in-state and out-of-state equipment and facilities in providing service[.]" Id.

No doubt recognizing that they cannot meet their burden under traditional commerce clause jurisprudence, appellants advance a novel and startling proposition – that state courts and legislatures must engage in a fact-intensive balancing test to determine which of two businesses is "more local." This remarkable proposition is wholly unsupported by United States Supreme Court precedent. Instead, the Supreme Court has repeatedly acknowledged in tax cases that "[t]he complexities of factual economic proof always present a certain potential for error, and courts have little familiarity with the process of evaluating the relative economic burden of taxes." *Minneapolis Star & Tribune Co. v. Minnesota Comm'r of Revenue* (1983), 460 U.S. 575, 589-90; see also *General Motors*, 519 U.S. at 309 ("We are consequently ill qualified to develop Commerce Clause doctrine dependent on any such predictive judgments, and it behooves us to be as reticent about projecting the effect of applying the Commerce Clause here, as we customarily are in declining to engage in elaborate analysis of real-world economic effects * * * *"). Appellants' novel proposition would require courts (and legislatures) to engage in precisely the sort of complex factual and economic analysis that the Supreme Court has counseled against.

Equally alarming to the Amici States, appellants' relative presence test is wholly unworkable as a practical matter. Appellants ask this Court to abandon the traditional view of the commerce clause (that States are precluded from discriminating against interstate commerce) and substitute a new untested and unapproved rule of law. This new rule would require States to first undergo fact-intensive economic and geographic analyses to determine which interstate companies have a greater local presence. If that arduous task revealed any differences in degree of presence – no matter how slight – the State would be precluded from taxing the companies differently, regardless of any differences in technology or business operations. Such a rogue construction of the commere clause would be completely unmanageable and devastating to the States.

The framers of the Constitution never anticipated nor intended that, before imposing a tax on a particular industry, a State's legislature would have to engage in a costly and time-consuming analysis of the extent of the local presence of every business potentially subject to the tax. Under appellants' theory, Ohio could not tax satellite television programming at a higher rate than cable television programming because cable television providers (who also are interstate companies) supposedly have a greater local presence than satellite television providers.[1] If, however, DirecTV were to move its Customer Contact Center in Huntington, West Virginia to Cleveland, Ohio, that analysis could potentially change mid-tax year. The State of Ohio cannot reasonably be expected to monitor the relative local presence of each and every industry that does business in the State in order to determine whom it may or may not tax. Significantly, appellants' new rule would not be limited to the provision of television programming. If adopted by this Court, that theory would force Ohio to reevaluate its entire taxation scheme, including for example the taxation of ground transportation services as compared to air transportation. A comparison of the "local presence" of countless interstate trucking firms versus scores of airlines would be an impossible undertaking and an unwarranted interference with Ohio's sovereign power to tax. The Constitution simply does not place such an onerous obligation on States.

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[1] Currently, satellite television providers have a substantial "local presence" in at least eighteen States: Alabama, Arizona, California, Colorado, Delaware, Georgia, Idaho, Illinois, Montana, Nevada, New Jersey, New York, Texas, Oklahoma, Virginia, Washington, West Virginia and Wyoming. (http://www.directv.com/DTVAPP (follow "Our Company" hyperlink at bottom of the page; then follow "Company Profile" hyperlink) and http://www.echostar.com/Company/Locations.aspx). The "local presence" of satellite television industry, of course, changes as the market share of the industry increases (thereby necessitating an increase in physical facilities such as customer contact centers) and as new satellite television providers enter the industry. Thus, the relative "local presence" of satellite television providers in a given State may change substantially within a period of months.

B. Cable Companies and Satellite Companies Are Not Similarly Situated for Commerce Clause Purposes

To succeed with their commerce clause challenge, appellants must convince this Court beyond a reasonable doubt that satellite companies and cable companies are similarly situated for commerce clause purposes. See *General Motors*, 519 U.S. at 298 ("any notion of discrimination assumes a comparison of substantially similar entities"); *Halliburton Oil Well Cementing Co. v. Reily* (1963), 373 U.S. 64, 70 (precondition for valid tax is "equal treatment for in-state and out-of-state taxpayers similarly situated"); *State ex rel. Dickman v. Defenbacher* (1955), 164 Ohio St. 142, 149, 128 N.E2d 59, 64 ("if under any possible state of facts the law would be constitutional, the court is bound to presume that such facts exist"). The rationale for the "similarly situated" prerequisite is simple: there is "[n]o iron rule of equality between taxes laid by a State on different types of business." *Alaska v. Arctic Maid* (1961), 366 U.S. 199, 205 (citation and internal quotations omitted). Thus, disparate treatment constitutes discrimination only if the objects of the disparate treatment are similarly situated. Here, appellants have not and cannot show that cable companies and satellite companies are similarly situated.

Critical distinctions exist between the satellite and cable industries which differentiate them for commerce clause purposes. Congress has acknowledged that the two types of companies are not similarly situated in at least two significant ways: Congress has ordained that cable companies may be taxed at the local level, while expressly prohibiting the taxation of satellite companies at the local level. Compare Pub. L. 104-104, 110 Stat. 56, § 602(c) with 47 U.S.C. § 542. Congress has also imposed public service obligations on cable companies that are vastly different from those imposed on satellite companies. Ohio Br. 14-15; see also 47 U.S.C. §§ 531(a), 534(b), 535(b), 543(b)(7), 544(g) (2006); 47 C.F.R. § 76.56 (2008). Where Congress has expressly chosen to treat the two types of businesses differently in significant respects – including the means by which States and localities can tax them – appellants cannot meet their burden to establish that the two are similarly situated for commerce clause purposes.

Also, the two industries use very different delivery technology to deliver their product. Ohio Br. 7-8. Here, therefore, "[w]hatever different effect the [tax provision] may have on these two categories of companies results solely from differences between the nature of their businesses, not from the location of their activities." *Amerada Hess Corp. v. Director, Div. of Taxation* (1989), 490 U.S. 66, 78. Because the two industries are not similarly situated, no impermissible discrimination exists.

C. <u>Appellants Have Not Empirically Demonstrated That the Tax Imposes a Cost Disadvantage on Satellite Companies and Therefore Have Not Proven Discrimination in Practical Effect</u>

Finally, even if appellants were somehow able to show that cable companies are a similarly-situated local interest in this case, they must provide "convincing evidence showing that the [Ohio] tax deters, or for that matter discriminates against, interstate activities." *American Trucking II*, 545 U.S. at 437. To satisfy its burden of proving that a tax discriminates in practical effect, a taxpayer is required to "*empirically * * * demonstrate* the existence of a burdensome or discriminatory impact upon interstate [commerce]." Id. at 436 (emphasis added). The Supreme Court has "never deemed a hypothetical possibility of favoritism to constitute discrimination that transgresses constitutional commands." *Associated Indus.*, 511 U.S. at 654. Instead, the analysis focuses on whether there is discrimination in practical effect – one that results in real injuries. Id.

Here, appellants have failed to demonstrate empirically that Ohio's tax scheme deters or discriminates against interstate commerce. Appellants summarily complain that "the State put its thumb on the scale of competition by raising satellite TV's price." Appellants' Br. 2. There is no evidence in the record demonstrating that appellants have suffered any real injuries, however. In fact, all available evidence establishes precisely the opposite.

Appellants blithely state that satellite subscribers are "slapped" with a sales tax, while cable subscribers are let off "without paying a penny of state tax." Appellants' Br. 1. Technically, this statement is true. What appellants conveniently ignore, however, is the fact that cable companies pay a local franchise tax that satellite companies do not pay.[2] Thus, each industry bears a tax burden unique to it. See *Halliburton Oil Well Cementing Co.,* 373 U.S. at 69 ("a proper analysis must take 'the whole scheme of taxation into account'").

Appellants some years ago unsuccessfully challenged, on commerce clause grounds, a North Carolina sales tax provision similar to the one at issue here. *DirecTV, Inc.*, 178 N.C.App. 659, 632 S.E.2d 543. Just as they do here, appellants asserted that the sales tax result[ed] in "a substantial cost disadvantage on satellite operators, and inhibit[ed] their ability to compete with cable companies." Id. at 668, 632 S.E.2d at 550. In the course of rejecting their arguments, the Court of Appeals observed that

> the record is void of any evidence that this tax has created an undue burden on interstate commerce. Even after the imposition of the sales tax in 2002, [the appellant satellite television providers'] number of subscribers and gross revenues have increased from 2001 to 2003 in North Carolina. Moreover, [their] share of the North Carolina

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[2] By explicit congressional design, States are authorized to tax satellite companies, and local governments are authorized to tax cable companies. Compare Pub. L. 104-104, 110 Stat. 56, § 602(c) (1996) with 47 U.S.C. § 542 (2006).

> multichannel video programming market has continually increased and has remained higher than their share of the national multichannel video programming market.

Id. at 668. The court concluded that the appellants' "success in this market with the imposition of the sales tax * * * defeats any claims that they are being discriminated against in its practical effect." Id.; see also *Prudential Insurance Co. v. Benjamin* (1946), 328 U.S. 408, 432 (business's continuous success refutes idea that tax handicapped it in any way). The court held that "[b]ecause Plaintiffs have failed to provide sufficient evidence that the tax discriminates against them in its practical effect, much less evidence so clear that no reasonable doubt can arise, [the North Carolina sales tax] must be sustained against their constitutional challenge." *DirecTV*, 178 N.C.App. at 668-69, 632 S.E.2d at 550.

Appellants' continuous success in the North Carolina marketplace mirrors their continuing success nationwide, undermining any argument of economic burden. According to a recent Federal Communications Commission ("FCC") report:

> Cable serves the largest percentage of MVPD [multichannel video programming distribution] subscribers, but cable's share of the MVPD marketplace continues to decline. As of June 2006, 68.2 percent of MVPD subscribers received video programming from a franchised cable operator, as compared to 69.4 percent as of June 2005. DBS [direct broadcast satellite] subscribers comprise the second largest group of MVPD households, representing 29.2 percent of total MVPD subscribers as of June 2006, compared to 27.7 percent in June 2005.

In re 13th Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming (2009), 24 F.C.C.R. 542, 546.

This increase in the market share enjoyed by DBS providers continues a trend that had been noted in the previous FCC report on the status of competition in the MVPD market. *In re 12th*

Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming (2006), 21 F.C.C.R. 2503, 2506-07. Read together, the two reports show cable's market share steadily declining from 71.6 percent in June 2004 to 69.4 percent in June 2005 and 68.2 percent in June 2006. Meanwhile, the market share of DBS providers – which is essentially the combined market share of the two appellants in this case – steadily increased from 25.1 percent in June 2004 to 27.7 percent in June 2005 to 29.2 percent in June 2006.[3]

According to the most recent FCC report, approximately 28 million households subscribed to DBS service as of June 2006. 24 F.C.C.R. at 580. This represented a 7.1 percent increase over the 26.12 million DBS subscribers in the previous year. Id. at 580-81. The report describes appellants' subscribership as follows:

> DIRECTV is the largest DBS provider and second largest MVPD. It served 15.51 million subscribers as of June 2006, an increase of 843,000, or 5.7 percent, from the 14.67 million subscribers it had as of June 2005. This compares with growth of 12.5 percent reported in the previous year. As of June 2006, EchoStar was the second largest DBS provider and third largest MVPD, with approximately 12.46 million subscribers as of June 30, 2006, an increase of approximately 1 million, or almost 9 percent, over the 11.45 million subscribers it had a year earlier. In 2005, EchoStar reported growth of 13 percent.

Id. at 581.

Significantly, "[a]nalysts attribute DBS's continued growth to higher than expected new subscribership, lower churn than expected for existing subscribers, and higher revenue yields per customer." Id. In the sections of the FCC reports entitled "Market Structure and Conditions

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[3] There are only three DBS operators licensed in the United States: DirecTV, EchoStar and Dominion Video Satellite. 24 F.C.C.R. at 580. Dominion serves fewer than 500,000 subscribers. Id. at 581.

Affecting Competition," there is no mention of state sales taxes as a barrier to competition by DBS providers. See id. at 622-65; 21 F.C.C.R. at 2570-97.

More importantly, appellants have provided no evidence that the tax at issue here has hampered their ability to compete in the Ohio market. The Ohio tax became effective June 26, 2003. Section 198(A), Am.Sub.H.B. No. 95. There is nothing in the record to indicate that the tax has adversely affected appellants since that time. In fact, from June 2003 to June 2004, the first year of the new tax, DBS providers' market share increased from 22.7 percent to 25.1 percent nationwide. *In re 11th Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming* (2005), 20 F.C.C.R. 2755, 2759. Appellants' subscribership also increased during this period:

> DIRECTV retains its position as the leading DBS provider and second largest MVPD with 13.04 million subscribers as of June 2004, an increase of 12.4 percent from the 11.6 million subscribers as of June 2003. EchoStar is the second largest DBS operator and fourth largest MVPD, with 10.12 million subscribers as of June 30, 2004, an increase of 15 percent over the 8.8 million subscribers as of June 2003.

Id. at 2793.

The United States Supreme Court has emphasized that, when challenging a tax on commerce clause grounds, the record must contain empirical evidence that the tax imposes a significant practical burden on interstate trade. *American Trucking II*, 545 U.S. at 434. Here, appellants have offered absolutely no empirical data to support their claims that the Ohio tax burdens or discriminates against interstate commerce. See, e.g., Appellants' Brief at 1 (the tax "*could* be enough to persuade [a hypothetical consumer] to choose cable TV over satellite TV") (emphasis added).

The Ohio Court of Appeals, the United States Court of Appeals for the Sixth Circuit, and the North Carolina Court of Appeals[4] all have rejected appellants' commerce clause challenges to allegedly discriminatory taxes on sales of satellite TV services. *DirecTV, Inc. v. Treesh* (C.A.6, 2007), 487 F.3d 471, 480, cert. denied (2008) 128 S. Ct. 1876; *DirecTV, Inc. v. Levin*, 181 Ohio App.3d 92, 2009-Ohio-636, 907 N.E.2d 1242; *DirecTV, Inc.*, 178 N.C.App. 659, 632 S.E.2d 543. This Court should hold that appellants have failed to meet their burden to demonstrate beyond a reasonable doubt that the Ohio tax discriminates against interstate commerce.

III. CONCLUSION

The decision of the Court of Appeals should be affirmed.

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[4] Appellants attempt to distinguish the North Carolina Court of Appeals decision by arguing that, in North Carolina, they "did not present the theory argued here, that the tax violated the Commerce Clause for the simpler reason that the imposition of the tax depended upon whether or not a particular activity was performed in state." Appellants' Br. 44. Appellants misrepresent the argument that they made in *DirecTV, Inc. v. State*. In that case, Appellants argued – just as they argue here – that the tax was unconstitutional because "[t]he tax's applicability depends on whether the seller performs a specified activity – distribution of television service 'directly' to customers – by using out-of-state 'satellites' or in-state 'ground receiving and distribution equipment.'" DirecTV and Echostar Br. 21 (*DirecTV, Inc. v. State*).

Dated: December 14, 2009

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing **BRIEF OF AMICUS CURIAE STATES IN SUPPORT OF DEFENDANT-APPELLEE** upon all parties by placing a copy of same in the United States Mail, first class postage prepaid, addressed to their ATTORNEYS OF RECORD as follows:

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I also sent courtesy copies to counsel of record for all known amici curiae.

This the 14th day of December, 2009.

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