No. 10-1322

IN THE
Supreme Court of the United States

DIRECTV, INC. AND ECHOSTAR SATELLITE L.L.C.,
Petitioners,

v.

JOSEPH W. TESTA, Tax Commissioner of Ohio,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO
THE SUPREME COURT OF OHIO

REPLY BRIEF FOR PETITIONERS

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INTRODUCTION[1]

This case presents three different visions of how the Commerce Clause should apply in an increasingly common situation: two businesses deliver the same product but use different business methods that bring vastly different economic benefits to the state. Plaintiffs believe that when the protectionist state favors the business that showers the state with economic benefits, it is almost a *per se* case of discrimination against interstate commerce in practical effect. The Commissioner asserts that the scenario can sometimes be a Commerce Clause violation, depending on the balance of unspecified "factors." And finally, the Ohio Supreme Court—the opinion that the Commissioner defends—treats the difference in economic footprint as an irrelevancy. This is not some academic quibble. It is a legal distinction that is outcome-determinative here and in the various other cases discussed in the Petition.

As to the second question presented, both sides agree: Of course, there can be a Commerce Clause violation where the beneficiaries and victims of a discriminatory regime are both major interstate companies. The Commissioner just denies that the Ohio Supreme Court adopted that principle. But the dissent below, dozens of constitutional law scholars, and various other amici read it that way—as will other courts and future litigants.

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[1] This brief uses the same abbreviations as the Petition. The Brief in Opposition is cited as "Opp." And amicus briefs are cited according to the name of the first party on the brief.

Both issues are splitting the courts and the Commissioner does not deny that they are important. This Court should grant certiorari.

ARGUMENT

I. THE QUESTIONS PRESENTED HAVE SPLIT THE COURTS AND MERIT THIS COURT'S REVIEW.

The Commissioner demonstrates the confusion that this Court's opinions have engendered on the first question presented and throws in the towel on the second. Both splits are real, important, and cert-worthy.

A. The Role Of Differing "Methods Of Operation" In Commerce Clause Analysis Is A Question Worthy Of Review.

1. The Commissioner highlights the confusion on "methods of operation."

Certain baseline principles are indisputable. First, Plaintiffs can prove a Commerce Clause violation based on discriminatory effect without proving (1) that the statute *explicitly* distinguishes in-state businesses from out-of-state-businesses or (2) that the state *purposefully* advanced its own economy at the expense of the economies of other states.

Second, a Commerce Clause challenge based on practical effects has three elements: (A) competition between two "substantially similar entities," *Gen.*

Motors Corp. v. Tracy, 519 U.S. 278, 298-99 (1997), or "similar products," *W. Lynn Creamery v. Healy*, 512 U.S. 186, 193 (1994); (B) the state treats these entities or products differently, *id.*; and (C) this differential treatment "'will in its practical operation work discrimination against interstate commerce,'" *id.* at 201 (quoting *Best & Co. v. Maxwell*, 311 U.S. 454, 455-456 (1940)). The Ohio Supreme Court disposed of this case on the last element (prong C), alone.

Third, as the Commissioner agrees, *see* Opp. 19, 27, a court cannot reject a claim of discriminatory effect without conducting "a sensitive, case-by-case analysis of [the statute's] effects." *W. Lynn Creamery*, 512 U.S. at 201.

The dispute is over what "effects" qualify as "discrimination against interstate commerce." Plaintiffs' position (which the dissent embraced, App. 24a) is that a statute has the practical effect of discriminating against interstate commerce when it favors a product that boosts the local economy—with buildings, infrastructure, jobs, and investment—over a competing product that does not.

The Commissioner has never disputed that cable has a vastly greater local economic footprint than satellite. But, like the court below, he treats it as an irrelevancy (his analysis never even mentions it), fixating instead on the technological differences between satellite and cable. He couches this theme in formulations that ricochet between two different elements of a Commerce Clause challenge—and between two of the camps described in the Petition.

At times, the Commissioner tracks the Ohio Supreme Court's approach of addressing the last element (prong C, above). Invoking *Exxon* and *Amerada Hess*, he argues that there is no discriminatory effect if the two competing "business[es] use different 'methods of operation' to provide *similar* products." Opp. 1 (emphasis added). The discrimination among similar products, he claims, is permissible so long as the operations "differ in *any relevant way*." Opp. 15 (emphasis added). That is the Camp 1 approach.

Contrary to the Commissioner's assertion, that is not what "[t]his Court has already held" in *Exxon* and *Amerada Hess*. Opp. 1. Those cases first conducted exhaustive analyses to conclude that there was *no evidence* that the statutory distinction benefited businesses that contributed more to the local economy, and only then, *based on that conclusion,* held that the statutes in question distinguished "*solely* between the nature of" the "businesses, *not* … the location of their activities." *Amerada Hess Corp. v. Dir., Div. of Taxation, N.J. Dep't of the Treasury*, 490 U.S. 66, 78 (1989) (emphasis added); *see* Pet. 13, 34-36. Like the Camp 1 cases, the Commissioner's "any-relevant-difference" formulation bypasses the critical first step of examining the relative effect of each competing product on the local economy.

At other points, the Commissioner follows Camp 3's approach, invoking those same two cases in support of the argument that Plaintiffs have failed a different element—that the products are "similarly situated" (prong A, above). He argues that those

same two cases "rejected discrimination claims involving *differently situated businesses,*" and that the same is true here. Opp. 13 (emphasis added). But that is not what the court below held. It took no issue with the trial court's holding that cable and satellite TV were similarly situated. App. 120-21a. And for good reason: This Court has held that the touchstone for determining whether two products are similarly situated is whether there is "actual or prospective competition between the supposedly favored and disfavored entities in a single market," *Tracy*, 519 U.S. at 300, and, as the trial court explained in an extensive analysis, cable and satellite indisputably are vigorous competitors selling virtually identical products to the same customers in the same market. App. 169-80a.

The difference between the Commissioner's two formulations—between Camp 1 and Camp 3—matters. Those two prongs serve different purposes and are infused with different policy rationales. *Compare Tracy*, 519 U.S. at 298-300, *with W. Lynn Creamery*, 512 U.S. at 201-02. And those differences do, and should, affect how the lower courts apply the principle. More importantly, the lower courts need this Court to clarify whether or not a difference in mode of operation affects a Commerce Clause claim at all, and if so, under what circumstances.

2. The lower courts are split on "methods of operation."

This case does not present an "academic" debate, Opp. 22, about an inconsequential "framework

error," Opp. 29. The different analytical approaches of the three camps are outcome-determinative.

Contrary to the Commissioner's contention, neither the Ohio Supreme Court nor any other court in ***Camp 1*** conducted "a comprehensive analysis of the law's effects." Opp. 19. None pursued an analysis that accounted for the very different extent to which the competitors on either side of the statutory divide *contribute to the local economy*. To the contrary, the Ohio Supreme Court's analysis of effects was encapsulated in two sentences: (1) "Here, the tax applies to a transaction involving pay-television services depending only on the technological mode of distribution of those services"; and (2) "Application of the sales tax does not depend on the geographic location of the programming provider." App. 16a. The Sixth Circuit similarly referred to the "effects" of the statutory provisions at issue only once, distinguishing a case that found discriminatory effect on the ground that: "In this case, however, the two 'goods' are distinct, consisting of two very different means of delivering broadcasts." *DIRECTV, Inc. v. Treesh*, 487 F.3d 471, 479-80 (6th Cir. 2007) (citations omitted). Likewise, the North Carolina court invoked the *Amerada Hess* principle about "'the nature of their businesses,'" *DIRECTV, Inc. v. State*, 632 S.E.2d 543, 549 (N.C. Ct. App. 2006) (citation omitted), and described *Exxon* and *Amerada Hess* at length, *id.* at 548-50. Then, without any reference to the vast difference in economic footprint, it concluded that the differential treatment was permissible because the tax "depends only upon how companies deliver television programming services to [their] subscribers." *Id.* at

550. Thus, our position on the opinion below (and its Camp 1 companions) is not a "quibble[] that the court's analysis" of the difference in economic footprint "was not deep enough," Opp. 21, but a complaint that it was deep-sixed.

The Commissioner fails to reconcile these cases with the diametrically opposite ***Camp 2***. He does not dispute that the Camp 2 cases usually analyze how the businesses on either side of a statutory line have vastly different economic ties within the state—and find that difference dispositive. He simply either misstates each court's analysis or emphasizes irrelevant distinctions—or both:

- The Commissioner asserts that the Eleventh and Seventh Circuits invalidated the statutes before them because those statutes "*banned*" certain types of businesses or activities. Opp. 29-30 (emphasis in original). But for purposes of determining whether a statutory distinction discriminates against interstate commerce, this Court has never distinguished discriminatory bans from discriminatory taxes or other burdens. Neither the Eleventh nor the Seventh Circuit found that distinction dispositive.

- The First Circuit's decision was not "based on discriminatory *purpose*," alone. Opp. 29 (emphasis in original). The First Circuit held that the law "violates the Commerce Clause because the *effect* of the gallonage cap is to change the competitive balance between in-state and out-of-state wineries." *Family*

Winemakers of Cal. v. Jenkins, 592 F.3d 1, 5 (1st Cir. 2010) (emphasis added).

- The Commissioner's only response to the Fourth Circuit case is that it found discrimination in practical effect, but "did not even cite *Exxon*, … nor did it refer to 'methods of operation.'" Opp. 30. Exactly our point.

The Commissioner tries to portray all the cases as fitting into ***Camp 3***. Opp. 27. But the only way he can do that is by mischaracterizing the common trait of Camp 3 cases. The courts in that camp do not consider operational differences "as part of a broader analysis," Opp. 27, but specifically in determining whether businesses are "similarly situated." As demonstrated above, that is not what the Ohio Supreme Court did. *Supra* at 6. Nor did any of the courts in Camps 1 and 2 address that prong.

Nevertheless, in an effort to reconcile all 13 of these cases, the Commissioner contends that they all treat "methods of operation" as a "factor," and reach different conclusions by "accord[ing] greater or lesser weight to th[at] factor[] … only because the facts of those cases raised or lowered the importance of" the competitors' respective economic footprints. Opp. 4 (emphasis omitted). But that only compounds the confusion. None of those cases says that the concept is a "factor" to be weighed. This Court has never treated "methods of operation" as a factor to be weighed along with others, but rather found it relevant only if it was the "sole[]" factor in play. *Amerada Hess*, 490 U.S. at 78. If the "method of

operation" is now a "factor" to be weighed, the lower courts need this Court's guidance on how much to weigh it and against what.

Finally, the court below did not join a "chorus of courts uniformly rejecting DIRECTV's similar claims regarding satellite and cable broadcasting." Opp. 3. As is evident from the Commissioner's citation to two appellate cases—from the Sixth Circuit and an intermediate state court—the divided court joined a duet.[2]

B. The Court Should Address How The Commerce Clause Applies Where Both The Victims And Beneficiaries Of A Statutory Distinction Are Major Interstate Businesses.

Through eight years of litigation, the Commissioner has argued, as it did before the Ohio Supreme Court, that the "Commerce Clause analysis with respect to the Satellite and Cable Companies need not go beyond the essential fact that both businesses are interstate businesses engaged in predominately interstate economic activity." Merits Brief of Defendant-Appellee at 23. The trial court rejected the proposition explicitly, App. 111-19a, but the intermediate appellate court explicitly adopted it, App. 53a.

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[2] The Fourth Circuit did not "reject[] the premise of DIRECTV's discrimination claim." Opp. 26. It dismissed the case for lack of jurisdiction. *DIRECTV, Inc. v. Tolson*, 513 F.3d 119, 128 (4th Cir. 2008).

Having persuaded the Ohio Supreme Court to adopt the principle, the Commissioner now refutes it, conceding that practical effect "claims can surely exist where all parties are interstate." Opp. 22. He argues instead that the court below said no such thing. *Id.* But there is no other way to interpret the two paragraphs in the Ohio Supreme Court's opinion explaining that "the cable industry is not a *local* interest"; that "[l]ike the satellite companies, the major cable providers are *interstate companies* selling an interstate product to an interstate market"; and that "no major pay-television provider is *headquartered in Ohio* or could otherwise be considered more local than any other." App. 16-17a (emphasis added).

The dissent read the opinion as we do, faulting the majority for "focus[ing] narrowly on the location of ownership or headquarters." App. 22a. That is how 42 constitutional law professors have read the passage, *see* Const. Law Profs. Br. 6, 9, 10, 19, as well as various other amici, *see, e.g.,* Nat'l Taxpayers Union Br. 4, 6-7; Specialty Wine Retailers Ass'n Br. 3, 16-17, and how every court and litigant will read it going forward.

The Commissioner does not deny that the principle all these observers see in the opinion below violates this Court's holdings or that the issue split the lower courts even before the Ohio Supreme Court weighed in. *See* Pet. 24-28. Nor does he deny that the principle would upend this Court's Commerce Clause jurisprudence and warrant this Court's review. This Court should grant certiorari to resolve the split and end the mischief.

II. THIS CASE IS A GOOD VEHICLE.

Contrary to the Commissioner's assertions, this case presents a perfectly suitable vehicle for resolving the questions presented.

The Commissioner begins with the erroneous contention that "DIRECTV does not ask this Court to find discrimination and rule in its favor," but "only for a remand" to apply a different test. Opp. 33. The Petition says nothing about a remand. Plaintiffs contend that the trial court, applying the correct standard, correctly granted summary judgment, finding discrimination in practical effect—and that an appellate court applying the correct analysis would uphold that ruling (as the dissent below advocated).

Equally erroneous is the Commissioner's contention that Plaintiffs do "not assert … that [their] case does *not* fall under *Amerada Hess*, or that it does fall under … any category of discrimination that this Court has described and condemned." Opp. 34 (emphasis in original). Our merits briefs make exactly those arguments at length, as does the dissent below, App. 21-27a, and the Petition summarizes the points, under the heading, "THE OHIO SUPREME COURT'S ANALYSIS IS WRONG," Pet. 33-39.

In particular, Plaintiffs have invoked cases such as *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984), and *Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388 (1984), which, we maintain, stand for the proposition that a state may not grant preferential tax

treatment to businesses that build certain facilities or perform certain functions within the state, over those that do not. The Commissioner tries to distinguish the entire line of cases by insisting that the rule applies only where the statute creates an "incentive to relocate"—i.e., where the state "reward[s] out-of-state companies if they merely shift[] their activities into the State with the discriminatory law." Opp. 16. But *Armco* struck a tax that created no "incentive to relocate." There, West Virginia was concerned about a tax levied on in-state manufacturers that was advantaging *out-of-state* companies. 467 U.S. at 642. So it adopted the challenged tax to offset the disparity, *id.* at 642—exactly what the Commissioner claims the satellite-only tax was designed to do. Opp. 1. The resulting regime gave an out-of-state company no incentive to relocate a manufacturing plant to West Virginia, because the goods manufactured domestically would have been subject to a different, and roughly equivalent, tax.

As discussed, *see supra* at 2, the Commissioner is also wrong to suggest that Plaintiffs' effects arguments cannot prevail without proof of discriminatory intent. Opp. 34-36. Nor does the Petition revolve around "concepts of intentional discrimination." Opp. 34. The Petition's occasional references to what the legislature hoped to achieve merely reinforce the undisputed evidence that it succeeded in achieving those effects.

Finally, the Commissioner offers a grab-bag of other merits arguments, revolving mainly around the regulatory differences between cable and

satellite. Opp. 36-38. Those differences would be relevant if—as in *Tracy*—they yielded a regime where (as the Commissioner puts it) the two businesses "sold [their product] to different consumer markets," and therefore did not compete for the same customers. Opp. 15; *see Tracy,* 519 U.S. at 300-10. But as the trial court explained at length, regulatory differences do not confine cable and satellite to different markets. App. 180-201a. More to the point, the possibility that regulatory differences might be relevant does not undermine the value of a decision in this case "for cases involving other industries." Opp. 36. Technological differences are often accompanied by regulatory differences. So whatever guidance this Court offers about the effect of regulatory differences on Commerce Clause analysis will be valuable to courts and litigants in many future cases. That is yet another reason to grant certiorari.

CONCLUSION

For these reasons, the Court should grant the petition for a writ of certiorari.

Respectfully submitted,

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