No. 14-1499

IN THE

Supreme Court of the United States

DIRECTV, LLC AND DISH NETWORK L.L.C.,
Petitioners,

v.

COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF REVENUE,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT OF MASSACHUSETTS

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF

In response to the petitions in this and the companion case,[1] the Court now has before it the arguments of not one, but two, state solicitors general. Those responses are filled with similar deficiencies that confirm the need for this Court's intervention. Neither Tennessee nor Massachusetts seriously denies the significance of the question presented—*i.e.*, how to assess when two entities are "similarly situated," such that substantive scrutiny under the dormant Commerce Clause is triggered. Instead, they downplay the split, and pivot to arguments about the ultimate merits. But precisely because the question presented here concerns a threshold issue, the merits arguments are not at issue (and the states' merits arguments are wrong anyway). The split is robust, and the states' arguments highlight the flaws in the decisions below.

On the state's telling, Commerce Clause analysis begins with a freewheeling inquiry into businesses' similarities and differences. If competing businesses are insufficiently similar, as measured by whatever hodgepodge of factors a particular court chooses to apply, then a state has free rein to tax and regulate them differently, no matter the impact on interstate commerce. This approach runs counter to the Court's precedents, and it has little to recommend it—not least because it will make analysis under the dormant Commerce Clause even less predictable.

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[1] Pet. for Writ of Cert., *DIRECTV, LLC v. Roberts,* No. 14-1524 (June 23, 2015) (hereinafter, "Tenn. Pet.").

Even so, this mode of analysis has been embraced by some courts, including the court below, and is the subject of a real and entrenched division of authority: Unlike the Massachusetts Supreme Judicial Court, other courts properly recognize that entities are "similarly situated" under the dormant Commerce Clause so long as they compete with each other. This competition-focused inquiry makes good sense; if two entities compete, then a state's decision to favor one over the other poses precisely the risk of economic protectionism that merits substantive scrutiny under the Commerce Clause. Discrimination may or may not ultimately be found, but that inquiry should not be cut prematurely short by a mini-merits inquiry in the guise of assessing whether businesses are similarly situated. The contrary approach, adopted below and defended by Massachusetts, injects portions of the merits into the threshold determination—and does so in a fashion that is incapable of principled application. This question merits review, now and in these cases.

ARGUMENT

I. The Split Is Real, And Lower Courts Need Guidance About What Makes Businesses Similarly Situated.

A. The overarching split

1. As we have explained, state and federal courts are nearly evenly split between two camps. Pet. 15-25; Tenn. Pet. 18-24; Tenn. Reply 3-6. Courts in the first camp correctly understand that the "similarly situated" requirement involves a straightforward,

threshold inquiry: Do the entities affected by an allegedly discriminatory state law compete in the relevant market? Upon resolving this (often easy) question, these courts consider (1) whether the challenged law differentiates between products or producers in a way that benefits in-state interests at the expense of out-of-state interests, and if so, (2) whether the state can prove that the discrimination is necessary to advance legitimate interests. *See* Pet. 16-20.

Meanwhile, courts in the second camp sweep in various factors that ought to be considered at later stages of the Commerce Clause analysis, and haphazardly invoke them as reasons for concluding that favored and disfavored entities are not similarly situated. Pet. 20-23. This is the camp with which the court below allied itself.

2. The state minimizes the split, insisting that courts in the first camp have not categorically declared that the inquiry "must be limited to whether entities are competitors." Opp. 13. On the contrary, these courts have spoken unequivocally: "Entities are 'substantially similar' or 'similarly situated' for Commerce Clause purposes when they compete against one another in the same market." *Smith v. New Hampshire Dep't of Revenue Admin.*, 813 A.2d 372, 377 (N.H. 2002).

The state insists that, because *Smith* concluded that the affected entities did not compete, it had no occasion to opine on whether other factors might be relevant. Opp. 17. In fact, *Smith* vividly illustrates the conflicting approaches. It involved a law that differentiated between banks and non-bank investment sources. The New Hampshire courts recognized the obvious: "banks differ from other business institutions." 813 A.2d at 377. The Massachusetts court would have stopped right there; after all, on the state's own telling, "differences between competing entities" render them not similarly situated for Commerce Clause purposes. Opp. 10. But the New Hampshire courts understood that this Court's precedents call for a competition-centered analysis. Thus, examining evidence developed at a multi-day trial, they ultimately concluded that the entities did not compete, and were not similarly situated. If it were enough to point to any old differences, this entire inquiry would have been unnecessary.

So too in *In re CIG Field Services Co*, 112 P.3d 138 (Kan. 2005). The inquiry there "centered" on competition and did not focus on "factors beyond market competitor status," Opp. 18, precisely because the parties and courts understood that this is how the analysis of "similarly situated" *should* work. 112 P.3d at 146 (focusing on whether the entities "serve[d] the same market"). The inquiry is not meant to catalogue the inevitable "differences in market competitors' circumstances." Opp. 15. Because the evidence established that, whatever their differences, the affected entities competed, the court held that they were similarly situated. 112 P.3d at 147 (upholding the finding that the entities "were competitive and thus similarly situated").

Family Winemakers of California v. Jenkins illustrates the conflict equally clearly. The First Circuit recognized that large wineries operate and are regulated differently from small wineries. 592 F.3d 1, 6, 14-15 & 16 n.18 (1st Cir. 2010). The reason the court was nevertheless able to "take[] for granted" that large and small wineries are similarly situated, Opp. 19, is that it did not inject these considerations into its "similarly situated" analysis. Instead, recognizing that large and small wineries were clearly "competitors," the court deemed them "similarly situated." 592 F.3d at 4-5, 10 (citing *General Motors Corp. v. Tracy,* 519 U.S. 278, 298 (1997); "any notion of discrimination assumes a comparison of substantially similar entities").

3. The state emphasizes that some courts in the first camp do not discuss the "similarly situated" requirement at length. Opp. 18-20. Exactly. That is because they understand, consistent with *Tracy*, that the "similarly situated" requirement is modest. "[M]ore often than not," *Tracy* explains, the matter can remain largely undiscussed because it is self-evident that the relevant entities are "substantially similar." 519 U.S. at 298-99. The "threshold question whether … companies are indeed similarly situated for constitutional purposes" does not even arise unless the entities "provide different products" and thus might "serve different markets, and would continue to do so even if the supposedly discriminatory burden were removed." *Id* at 299. That is why courts in the first camp appropriately limit their analysis to instances in which there is a real question about competition; camp two courts, in contrast, have turned the "similarly situated" inquiry into a centerpiece of Commerce Clause analysis. The conflict is very real.

B. The cable/satellite split

According to the state, "Petitioners' challenges to taxes on satellite … have all ended in the same final result," and this, the state says, shows that there is no "split on the main question presented." Opp. 10. That is a non sequitur. The "main question" here is the legal standard for assessing whether businesses are similarly situated, not whether "a state's taxing satellite and cable providers differently … run[s] afoul of the dormant Commerce Clause's bar on discrimination." Opp. 10. The latter is the ultimate question under the dormant Commerce Clause, and it is the one that the Massachusetts court declined to reach because it applied the wrong legal standard to the threshold analysis of "similarly situated." A further conflict within a particular factual context may supplement the case for review, but it is not necessary.

In any event, these cases do present such a context-specific conflict. Pet. 23-25. As the state acknowledges, Opp. 12, the Florida Court of Appeals recently held that cable and satellite providers are similarly situated because, despite using different technologies, they "operate in the same market and are direct competitors within that market." *DIRECTV, Inc. v. State of Fla., Dep't of Revenue*, Nos. 1D13-5444, 1D14-0292, __ So.3d __, 2015 WL 3622354, at *4 (Fla. Dist. Ct. App. June 11, 2015), *appeal docketed*, No. SC15-1249 (Fla. July 7, 2015); *see also id.* ("[M]ere differences in how a service is provided is not enough to overcome the fact that the companies compete in the same market and sell virtually identical products at retail."). The court went on to conclude that Florida's differential pay-TV tax scheme was unconstitutional.

Whatever the Florida Supreme Court ultimately decides, the Florida court's decision confirms that the "similarly situated" question raised here is not merely academic: When a court conducts a proper, competition-oriented "similarly situated" analysis, satellite providers are able to prevail not just on that threshold issue, but on the ultimate merits as well. And the Florida appellate court is not alone in so concluding. The Tennessee court outright rejected or cast serious doubt on the state's most serious merits arguments. Tenn. Pet. App. 15a-21a. And the most thoughtful opinions addressing satellite's challenges to unequal pay-TV tax schemes have found Commerce Clause violations—further giving the lie to the idea that the courts have been uniform. *See* Tenn. Pet. App. 35a-74a (Tennessee Chancery Court); *DIRECTV, Inc. v. Levin*, 941 N.E.2d 1187, 1197-1202 (Ohio 2010) (Brown, C.J., dissenting); *DIRECTV v. Wilkins*, No. 03CVH06-7135 (Ohio Ct. C.P., Franklin Cnty., Oct. 17, 2007).[2]

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[2] Moreover, the courts that have rejected satellite's claims have differed in their reasoning, confirming the confused state of Commerce Clause doctrine. Only the Tennessee and Massachusetts courts based their rejection on the "similarly situated" requirement, and even those rulings are not fully in accord. *Compare* Tenn. Pet. App. 29a-31a (relying on differing federal regulations), *with* Pet. App. 14a-18a (invoking other factors, such as the court's perception of the tax scheme's overall fairness). The other decisions cited by the state (Opp. 10-11) breezed past the threshold "similarly situated" inquiry and ruled on other (erroneous) grounds. The Ohio Supreme Court majority, for instance, did not dispute the dissent's

II. The Decision Below Is Wrong, And The State's Efforts To Defend It Underscore The Need For Review.

The state's efforts to defend the decision below highlight the profound confusion among lower courts. Like the Massachusetts court, the state embraces the mistaken premise that just because a court concludes that two entities are similarly situated means that the entities "must be treated alike." Opp. 13; *see also* Opp. 26. This characterization confuses the threshold, "similarly situated" inquiry with the ultimate questions of discrimination and justification. A law that differentiates between similarly situated entities sometimes will be held unconstitutional—but only if it discriminates against interstate commerce, and the state fails to prove the discrimination necessary to advance its legitimate interests. Courts confuse the law when they collapse these inquiries, and they weaken the Commerce Clause when (as here) they uphold laws that differentiate among competitors merely by pointing to operational or regulatory differences between them.

Tracy proves the error in the decision below. It makes clear that the purpose of asking whether differently treated entities are "similarly situated" is to

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assertion that the requirement that the "favored and disfavored parties be similarly situated" was easily met, "as cable and satellite unquestionably compete." *Levin*, 941 N.E.2d at 1201. The majority instead concluded that Ohio's differential pay-TV tax did not have a discriminatory effect—a determination that the Tennessee Court of Appeals later explicitly criticized. Tenn. Pet. App. 20a-21a & n.9. In short, what the pay-TV decisions reveal is not uniformity, but a mess.

ascertain whether they compete in the relevant market, such that "eliminating the [differential] tax … would … serve the dormant Commerce Clause's fundamental objective of preserving a national market for competition." 519 U.S. at 299. *Tracy* did not look to factors other than competition. It simply recognized that, when two entities compete only in a minor secondary market, not in the primary market, additional analysis may be needed to decide whether to "accord controlling significance" to the competitive or noncompetitive market. *Id.* at 303-04. That unusual situation is not present in this case.[3] Here, there is only one market, and it is undisputedly, fiercely competitive. In analogous situations, this Court has long focused its threshold inquiry on competition alone. *E.g.*, *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 269 (1984); *Alaska v. Arctic Maid*, 366 U.S. 199, 204 (1961).

The state further underscores the confusion between a threshold question and the merits when it invokes *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117 (1978), and *Amerada Hess Corp. v. Director, Division of Taxation, N.J. Department of Treasury*, 490 U.S. 66 (1989), and packages them with *Tracy* as a trio of cases that define the "similarly situated" in-

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[3] Nor does this case involve competition between public and private entities, as in *United Haulers Ass'n v. Oneida-Herkimer Solid Waste Management Authority*, 550 U.S. 330 (2007), and *Department of Revenue v. Davis*, 553 U.S. 328 (2008). *Cf.* Opp. 26. Those cases merely recognize that "[s]tates and municipalities are not private businesses" and need not treat themselves as such. 550 U.S. at 342-43. They do not displace the competition-centered analysis that applies when laws favor some private entities over others.

quiry. Opp. 14-15. Neither *Exxon* nor *Amerada Hess* turned on the "similarly situated" inquiry—or even uttered that phrase. Instead, both cases addressed the separate, subsequent question of whether the challenged laws discriminated against interstate commerce. In *Exxon*, the disputed law, which prohibited gas producers from owning gas stations, did not function as a local preference. It did not favor in-state gas production (Maryland had no gas reserves), and there was no evidence that it would disadvantage non-locally owned gas stations. 437 U.S. at 126 & n.16. *Amerada Hess* similarly determined that the disputed law did not distort the market in favor of local interests. 490 U.S. at 75-78.

Most telling of all, in neither case did the Court say that the Commerce Clause claim failed at the outset because the favored and disfavored entities operated differently. The entities competed, so the Court considered whether the laws were protectionist. The court below, in contrast, simply pointed to differences between cable and satellite and called it a day. This Court has never endorsed this approach, and the fact that litigants and some courts misread *Exxon* and *Amerada Hess* to do so is all the more reason for the Court to step in.

III. These Cases Are The Right Vehicle For Addressing This Important Issue.

Like Tennessee, Massachusetts does not seriously dispute the significance of this issue. Nor could it. Collectively, these cases affect tens of millions of U.S. households that subscribe to pay-TV service, and the question presented has significant implications for numerous other industries, especially ones in which innovative upstarts threaten entrenched and politically powerful local competitors. Pet. 34-37.

Instead, the state argues that there is an "independent basis for affirming the judgment below," Opp. 2—namely, that "neither cable nor satellite providers represent an 'in-state' economic interest, and thus no unlawful discrimination … takes place." Opp. 21. But this is a merits question that the court below did not reach. Indeed, the court assumed "that the cable companies and the satellite companies represent in-State and out-of-State interests, respectively." Pet. App. 13a.

The argument also is wrong. It depends on the mistaken notion that the Commerce Clause is offended only when a state protects "actual local companies." Opp. 25 n.9. This Court has never limited the Clause in this fashion, and doing so would render it a virtual dead letter. After all, few modern-day businesses are truly, exclusively local. The Court's cases make clear that states cannot favor businesses that perform activities locally over competitors that do not, and this is true regardless of where the benefited and burdened companies are headquartered, or whether they are small enterprises or large interstate conglomerates. *E.g.*, *Armco Inc. v. Hardesty*, 467 U.S. 638, 640-41 (1984) (invalidating West Virginia wholesale tax that exempted all businesses that performed manufacturing activities in the state, no matter their domicile); *Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388, 400-01 & n.9 (1984) (invalidating New York law that awarded tax credits to interstate companies only to the extent they performed their shipping activities within the state); *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 333-34 (1977) (invalidating New York law that taxed interstate stock transactions more favorably if the shares were transferred in New York). As in these cases, Massachusetts' satellite-only excise tax is unlawful because it favors businesses that build infrastructure within the state to assemble and distribute pay-TV packages over those who do not.[4]

If anything, the "actual local companies" argument strengthens the case for review. While most courts to consider the argument have properly rejected it—including in the case underlying the companion petition, *see* Tenn. Pet. App. 21a—a minority have accepted it, *e.g.*, *Levin*, 941 N.E.2d at 1196. That acceptance is further evidence of the persistent confusion surrounding nearly every aspect of this area of law, and serves to highlight the need for the Court's intervention.

CONCLUSION

For the foregoing reasons, the Court should grant the petition for a writ of certiorari; or, in the

[4] The state also contends that "neither this Court nor any other court has ever held that relative economic impact is the governing standard" for Commerce Clause discrimination. Opp. 22. But the satellite providers' theory of discrimination is not that "cable's relatively greater local economic activity makes it the 'local' concern." *Id.* It is that Massachusetts's differential tax rewards the business that performs certain activities and maintains certain facilities in-state (cable), and penalizes the one that does not (satellite).

alternative, grant the companion petition and hold this one.

Respectfully submitted,

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