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Before the
House Finance Committee
on Sub. H.B. 64

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Chairman Smith and members of the Committee, thank you for the opportunity to provide testimony regarding Sub. HB 64. My name is Jonathon McGee. I am the Executive Director of the Ohio Cable Telecommunications Association, a trade association representing cable television operators, programmers, and suppliers. Our member companies serve the majority of approximately four million cable television households in the state. On behalf of our customers and 8,000 full-time cable employees, I want to thank you for removing the imposition of a new sales tax on cable television service that was contained in the introduced version of HB 64. I am here today to briefly respond to several allegations which were made by my members' largest competitor, the Direct Broadcast Satellite (DBS) industry, in testimony on Wednesday.

It is certainly true that cable and DBS are taxed differently in Ohio. As I have testified in the past, cable is taxed at the local level through the state video service provider (VSP) fee. The video service provider fee is provided for in state law (ORC 1332.32), is set by the local governmental authority at a rate that can exceed 5%, and is collected by the local government. On the other hand, satellite service is taxed at the state level through the state sales tax of 5.75%. While these taxes are not identical, they are comparable. The satellite industry challenged this tax structure in 2003, only to have its challenge rejected by the courts.[1]

The disparity in this tax structure stems from Congress' 1996 attempt to shield DBS providers from the *administrative* burden of filing tax returns with thousands of local governments across the United States by preempting local taxation. Section 602 of the Telecommunications Act of 1996 (Pub. L. No. 104-104, Title VI, § 602 (reprinted at 47 U.S.C. § 152, note)) ("Section 602"). Congress was clear that it did not intend that DBS customers should pay ***less*** tax than cable customers. To that end, Section 602 specifically provides states with the authority to impose a tax on satellite companies and distribute the tax proceeds to local governments if they choose to do so.

Today, the two DBS providers are Fortune 500 companies with about one-third of the market; but DBS's local tax preemption remains in place despite the fact that the reason for the preemption (sparing fledgling companies a burdensome tax compliance obligation) has long

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[1] The current sales tax was imposed on DBS in 2003. At that time, the General Assembly decided not to tax the cable product, recognizing that doing so would amount to double taxation of cable. The DBS industry challenged this tax structure in court, with the Ohio Supreme Court upholding the law as being constitutional. The United States Supreme Court refused to hear the DBS industry appeal. *DIRECTV v. Levin*, 128 Ohio St. 68, 941 N.E.2d 1187 (2010), *cert. denied,* 133 S. Ct. 51, 183 L. Ed. 2d 675, 80 U.S.L.W. 3707 (2012).

since expired. As a result of this reality, the Ohio General Assembly in 2003 equalized the tax laws that historically favored the DBS industry and its subscribers. The General Assembly recognized that the state was already taxing cable through its local subdivisions under the franchise fee (now VSP fee). In correctly reading Section 602, the legislature realized that the proper taxing jurisdiction for DBS was the state.

Make no mistake, the Video Service Provider Fee and the state sales tax on DBS are both creatures of the Ohio Revised Code. This body chose to levy these taxes recognizing that sound tax policy demands that consumers be provided with a tax-neutral choice and that functionally equivalent services should be taxed in a similar manner. Sub. HB 64 maintains this tax policy goal.

When our competitors testified, they relied upon the canard that the VSP fee is somehow "rent" paid to local government for the use of the rights-of-way. However, the VSP fees are not rent to occupy the rights-of-way: the VSP fees are not based upon the cost to occupy the ROW as is required under Ohio law for municipal right-of-way charges -- instead, VSP fees are based on a percentage of the customers' bills on items that have nothing to do with the ROW.[2] Further, if the VSP fee was for the cost of occupying the rights-of-way, then all occupiers would pay this fee, but the VSP fee is unique to cable.

Moreover, even the courts have rejected arguments that fees like the VSP fee are "merely rent" for using "public spaces," holding instead that "franchise fees and related obligations are ... *not* rent payments, but rather statutorily authorized tax payments." *DIRECTV, LLC v. Dep't. of Revenue*, 2014 WL 7883570 at *5 (Mass. Feb. 18, 2015) ("*Massachusetts DBS Tax Case*") (emphasis added).[3]

DBS also mistakenly characterizes cable operators' franchise agreements, or, in Ohio's case, Video Service Authorizations as valuable "assets" based upon certain federally mandated filings. The accounting treatment of the massive investment by cable operators in their plant and equipment must appear on a balance sheet in some form as an asset, but bear in mind the right to provide service under the VSA is non-exclusive, subject to competition from DBS and telephone companies. DBS's citations to cable companies' annual reports show that "assets" are accounting entries derived from acquisitions and that, unlike any traditional "asset," are neither depreciated nor amortized. A review of two DBS annual reports shows identical treatment of the DBS providers' FCC satellite licenses. These are not "rent" for the orbital slots where their satellites are parked (indeed DBS occupies these invaluable slots for free) but reflect acquisitions, infinite

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[2] For example, cable pays VSP fees on (a) recurring monthly video service charges; (b) event-based charges (e.g., pay-per-view and VOD); (c) set-top box rentals and other video service equipment fees; (d) service charges relating to video service (e.g., activation, installation and repair); (e) administrative charges relating to video service (e.g., service order and service termination charges); and (f) advertising revenues, if a municipality or a township elects to include them. O.R.C. § 1332.32(B).

[3] In upholding the DBS excise tax in Massachusetts that did not apply to cable, the Supreme Judicial Court "follow[ed] the other courts that have considered and rejected the satellite companies' challenges to the laws of other States," and cited with approval the decision upholding the DBS sales tax here in Ohio. *DIRECTV, LLC v. Dep't. of Revenue*, 2014 WL 7883570 at *5, citing *DIRECTV v. Levin*, 128 Ohio St.3d 68, 941 N.E.2d 1187 (2010), *cert. denied,* 133 S. Ct. 51 (2012).

life, and goodwill. All in all, accounting entries like these have absolutely no bearing on the propriety of a tax policy.

One final argument made by the DBS operators in their oral testimony this week misleadingly suggests that their signals are delivered from satellites to customers without imposing *any* burden on the state or its municipalities, and, therefore, they should not be subject to state taxation. But DBS fails to note the many and varied ways in which their facilities are actually present in, and impose a burden upon, local communities. For example:

- DBS operators maintain extensive networks of local retailers and installers (such as the gentleman who testified on Wednesday) that must deliver and install specialized receiving equipment to enable DBS subscribers to receive satellite transmissions.

- Likewise, DBS operators, just like their cable competitors, must establish local antennae to receive the signals of local broadcast television stations and then distribute them to their subscribers. Those signals are obtained either by direct fiber optic links (consisting of fiber optic cables deployed on utility poles or in underground conduits) or over-the-air links between the DBS operators' satellite uplink sites and the broadcast television stations' studios.

Thus, while DBS uses a different ultimate delivery system than cable television, its local activities throughout Ohio all impose physical and regulatory burdens on the state and its communities. Even if cable did burden the local communities more than DBS, the legislature would still not be required to impose a greater tax burden on cable operators.[4]

DBS also argued that Ohio is somehow an "outlier" in its treatment of taxing these two competitors. But that is simply not the case. At least twelve states, including our neighbor Kentucky, have in some way enacted laws in an attempt to bring parity to the taxation between these video service providers.

Finally, any discussion of parity in the video industry should also include the disparity between cable and DBS regulation. Under Ohio law, cable operators are regulated by the Ohio Department of Commerce and support its activities financially, are subject to consumer protection statutes, and are required to set aside prime channel space for PEG channels – all of which are not applicable to DBS. At the federal level, DBS operators are treated more leniently than cable in a number of respects. If DBS is serious about parity, the imbalance of regulatory burdens should also be considered.

Chairman Smith, when the General Assembly placed the state sales tax on satellite service in 2003 it was in fact leveling the playing field between the two largest providers of multi-channel video service in Ohio. What the DBS industry is trying to get you to do is to upend sound public policy put in place by this body. We urge you to reject these arguments and to maintain Ohio's sound tax policy contained in current Ohio law and reflected in the substitute bill.

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[4] *Massachusetts DBS Tax Case* at *8 n. 15, citing *DIRECTV, Inc. v. Treesh*, 487 F.3d 471, 479 (6th Cir. 2007).