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**Before the Select Committee on Budget and Tax Reform  
Roundtable on Modernizing New York State's Telecommunications Taxes**

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Chairwoman Krueger, and members of the Select Committee on Budget and Tax Reform, thank you for the opportunity to participate in today's roundtable on modernizing New York State's telecommunications taxes. My name is Jeremy Kudon, and I am an attorney at Orrick, Herrington & Sutcliffe LLP in New York. I am here today on behalf of DIRECTV and DISH Network, the two major providers of satellite TV service in New York, and the Satellite Broadcast and Communications Association, a national association that represents all segments of the consumer satellite industry.

When it comes to pay TV service, we believe *New York's current tax structure for is fair and reasonable*. Pay TV is not subject to the "differing tax treatments" that plague other telecommunication services. To the contrary, all providers are treated exactly the same: New York does not impose state or local sales tax on pay TV—regardless of the provider. While some pay TV providers may pay more than others in property taxes, those taxes are based on about as objective a criteria as possible: the value of property each provider has in the State.

My clients provide pay TV service to over 1 million households in New York. The majority of these subscribers chose DIRECTV and DISH because of their lower prices, higher quality, and better service. Others—particularly families living in rural parts of the State—subscribe to satellite TV service out of necessity. The cable industry has made a conscious decision not to provide service to those families due to the cost of laying its wires and cables in less populated areas. Satellite TV is also the only option for the hundreds of thousands of New Yorkers

in Manhattan, Queens, and Staten Island, who rely on satellite TV for Russian, Greek, and Korean language programming, to name but a few.

We applaud the Committee's efforts to look at ways to modernize telecommunications' taxes. No one should be able to base an entire advertising campaign, as we saw with the Sir Charge ads, on the disparity between the taxes and surcharges paid by two providers of the same landline telephone service. But that discussion is better left to the other participants on the Roundtable. Unlike Verizon and Time Warner Cable, both of whom provide multiple telecommunication services, my clients only provide a single service to New Yorkers: Pay TV. Thus, my comments today will be limited to that service.

I would like to focus on three principles that we believe should frame any discussion on the taxation of pay TV service in New York:

- First, this is the wrong time to impose any new tax on pay TV service. In this current economic climate, we believe that the best recommendation this Committee can make when it comes to the taxation of pay TV is to maintain the status quo. As the old saying goes, "if it ain't broke, don't fix it."
- Second, if the Committee does recommend a new tax on pay TV, the tax should be imposed equally on all pay TV providers. It certainly should not be used to offset the franchise fees that cable companies pay to local towns and cities as "rent" to access the public rights of way necessary to deliver their video programming to subscribers.
- Third, the Committee should ensure that any discussion of a new tax on pay TV passes constitutional muster. The Ohio Supreme Court is poised to rule on the constitutionality of a 5.5% satellite-only state sales tax. If Ohio loses, and many commentators believe it will, it will be forced to refund over \$250 million to satellite TV subscribers. New York cannot afford this risk in this climate.

**A. Now is Not the Time to Impose New Taxes on Pay TV.**

The legislature and the Governor got it right in March. Now is not the time to impose a new tax on television. TV is no longer a luxury for most New Yorkers, it is a necessity. It's the primary source of information for everything from local news and weather to national politics and sports. When times are tough and wallets are thin, TV is the entertainment of last resort for millions of New Yorkers. We can cut out restaurants, we can rule out plays, movies, lectures, and sporting events as luxuries. And when we do, we stay at home, and click on the TV. Taxing this essential service threatens the quality of life of millions of

hardworking New Yorkers who are still dealing with the challenges of a recession that shows no signs of ending any time soon. It is a regressive tax that hurts those who can least afford it.

A cynic would say, “Broadcast TV is fine. Let them use rabbit ears.” Tell that to a Russian family in Brighton Beach or a Greek immigrant in Jackson Heights—or the hundreds of thousands of other New Yorkers who subscribe to a foreign language package. Pay TV service, and satellite TV in particular, is the only way for many of these families to get news, weather, or entertainment in a language they understand. Tell it to the tens of thousands of New Yorkers, many of whom live in the less populated parts of the state, who cannot get anything more than a fuzzy signal on the clearest day using rabbit ears.

#### **B. Any Tax on Pay TV Should Be an Equal One.**

If the Commission was to recommend a new tax on pay TV, we believe it must be premised on a simple principle: **Tax the service and not the provider.** Again, we believe this principle is already followed in New York when it comes to pay TV. But we should be clear what this means. It means imposing the same tax on all providers of pay TV service. It does not mean imposing a tax on one provider that is used to offset or cover expenses that are unique to another provider. Accordingly, we strongly urge this Committee to reject any proposal that would impose a tax only on satellite TV as an effort to offset the negotiated franchise fees that cable and phone companies pay to access the public rights of way.

Now, the cable industry may respond that franchise fees *are* taxes. It may argue, as it has in the past, that “tax parity” requires the State to levy a 5% tax on satellite TV customers to offset the amount it pays in local franchise fees. So which is it—a fee or a tax? Several authorities on the subject had this to say:

- “Franchise fees . . . are commonly understood to be consideration for the contractual award of a government benefit.”
- “[F]ranchise fees [are] a form of ‘rent.’”
- Cable’s “largest asset[s]” are “cable franchise rights” purchased with franchise fees.
- In contrast, “[t]axes simply have no contractual element; they are a demand of sovereignty.”

Are these the words of satellite TV partisans? No. These are the words of *cable companies*. They are taken directly from their SEC filings, franchise agreements, and briefs that they file with state and federal courts.

The bottom line is that franchise fees do not look anything like taxes. Consider the facts:

1. Local governments do not impose franchise fees the way they impose taxes. Telephone and cable companies voluntarily undertake to pay these fees as part of a negotiated contract.
2. Telephone and cable companies pay these franchise fees in return for a direct benefit—a property right—that they alone, enjoy. Not just anyone can dig up a public street or hang wires from a public utility pole. Local governments own that property, and they charge rent for it.
3. The property rights that phone and cable companies buy with franchise fees are highly valuable. Certainly the cable companies treat them as prized assets.
4. The franchise agreements that are negotiated at arms-length between cable and local governments look nothing like tax codes. They are intricate contracts that include all sorts of terms that one would never find in a tax code.

You don't call it a "tax" when a merchant pays rent for the right to set up a bodega on public property or a hot dog stand outside of the Metropolitan Museum of Art. You don't call it a "tax" when an advertiser pays to post an ad on the side of a bus or on the subway. And it is not a tax when cable negotiates an arms-length contract to purchase prized property rights necessary to sell its service. Here's how one cable company described "franchise fees" in a brief that it filed with a federal court of appeals:

Municipal franchises have long been understood to be contracts. Franchise fees, in turn, are commonly understood to be consideration for the contractual award of a government benefit. Many cases have treated franchise fees as a form of "rent." Cable franchises are enforceable as contracts, even though they are traditionally awarded by ordinance. . . . The contractual nature of cable franchise fees removed them far from "taxes." Taxes simply have no contractual element; they are a demand of sovereignty.

The consent of the taxpayer is not necessary to their enforcement.

Exhibit A at 15 (internal quotations and citations omitted). We could not say it any better ourselves.

In light of this evidence we strongly urge the Committee not to offset franchise fees that cable and phone companies pay to local towns and cities with an equivalent tax on satellite TV service. My clients have developed an innovative technology that does not require them to dig up public streets or hang wires from public utility poles to deliver their signals to subscribers. Making our customers pay a tax that is then used to purchase the property rights used by our competitors is no different than making airline passengers pay a tax for the use of railroad tracks: They don't use them, they shouldn't have to pay for them.

Nor should the Committee recommend a tax scheme that would abolish franchise fees and replace the revenue lost by local municipalities with a uniform sales tax on all pay TV subscribers. This scheme, which has been enacted in some form by North Carolina, Kentucky, and Virginia, forces satellite TV subscribers to pick up a portion of the tab—a tab negotiated by cable and phone companies—for those companies' right to access the public rights-of-way. The result is the same as taxing satellite TV more than cable. Discrimination is discrimination, even when it is veiled.

Our subscribers know the difference between a fair tax and discriminatory tax. For the past six months, the cable industry has deployed lobbyists across the country to press for new taxes on its main competitor—satellite TV. They've tried to slip the tax into budget bills in Vermont, New York, Texas, Nevada, Indiana, and Iowa, among others. With the exception of Massachusetts, every legislature to confront this sort of discriminatory proposal this year—eight in all—slapped it down. They listened to the thousands of calls they received from their constituents, urging them not to levy a discriminatory tax on satellite TV, a measure that many called a “Tax on Air.” And in every state but one, they saw these tax discrimination proposals for what they really are—a bailout for a cable industry that is losing ground in the marketplace. Now, Massachusetts is in the same position as Ohio and Florida, praying that a court will not order them to refund every penny that it collects from satellite TV subscribers in discriminatory taxes.

C. The Committee Should Ensure That Any New Tax On Pay TV Service Passes Constitutional Muster

Before reaching any conclusion on how to modernize the New York tax regime on telecommunications services, the Committee should carefully consider

the potential legal ramifications of any recommendation. Just ask Ohio. Six years ago the Ohio Legislature succumbed to cable's entreaties to impose a discriminatory tax in that state. The state tax commissioner warned that the tax was illegal, but the Legislature turned a deaf ear. It is now regretting the decision. After years of litigation, a respected Ohio trial judge struck the discriminatory law as unconstitutional—and ordered the state to refund every penny of the \$200 million it had illegally collected over the years. After a questionable reversal by an intermediate appellate court, the Ohio Supreme Court has agreed to hear the case, and is expected to issue a ruling on the constitutionality of the tax in Spring 2010.

To avoid years of costly and time consuming litigation and potentially refunding all revenue generated from a tax, we urge this Committee to carefully examine the constitutional issues presented by any proposed tax scheme before recommending it to the full Legislature.

Thank you for your time and attention. I look forward to discussing my testimony in greater detail during the Roundtable discussion.