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DaimlerChrysler v. Cuno: An Escape From the Dormant Commerce Clause Quagmire?

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DAIMLERCHRYSLER V. CUNO: AN ESCAPE FROM THE DORMANT COMMERCE CLAUSE QUAGMIRE?

I. INTRODUCTION

In March 2003, Philip Morris, America's largest cigarette maker, announced that it was moving its corporate headquarters from New York City to Richmond, Virginia.[1] The company resisted offers for relocation for nearly ten years, but a renewed and vigorous recruitment effort by Virginia Governor Mark R. Warner and local economic development officials persuaded the company to leave New York City.[2] Philip Morris hoped to bring an estimated 450 employees to Richmond.[3] Philip Morris's relocation to Richmond was a blockbuster deal for both the company and the region.[4] The company planned to invest nearly $50 million for construction on new buildings and $250 million on machinery and tools.[5] Convincing Philip Morris to move its corporate executives

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1. John Reid Blackwell, *Tobacco Town, USA; Philip Morris USA Will Move its NYC Headquarters Here in June*, RICH. TIMES-DISPATCH, Mar. 5, 2003, at A1.

2. *See* Bob Rayner, *Wooing Started in 1994; Warner Reignited Philip Morris Effort*, RICH. TIMES-DISPATCH, Mar. 6, 2003, at A1.

3. Blackwell, *supra* note 1, at A1. At the time of the announcement, Philip Morris already employed nearly 6800 people in the Richmond area. *Id.* By the end of 2003, nearly forty percent of the company's 680 New York City employees had decided to relocate with the company to Richmond. *See* John Reid Blackwell, *'Big Fish in a Smaller Pond'; Philip Morris USA Employees Move into New Headquarters*, RICH. TIMES-DISPATCH, Dec. 15, 2003, at D14.

4. Philip Morris estimated that it would save more than $60 million per year by moving its headquarters to Richmond. Blackwell, *supra* note 3, at D14. A significant amount of the savings would come from its real estate deal. *See* Terry Pristin, *Philip Morris USA Starts its Move to a Historic Building*, N.Y. TIMES, Nov. 26, 2003, at C5. Philip Morris gave up its Park Avenue address for a four-story, 250,000 square foot building on West Broad Street. *Id.* In 2001, the University of Richmond purchased the building from the Alcoa Corporation. *Id.* From the time the university purchased the building until Philip Morris moved, the building had been unoccupied. *See id.* Although the financial figures were not disclosed, it has been estimated that Philip Morris paid the University of Richmond between $16-$18 per square foot for its new office building, a paltry sum compared to $59 per square foot, the average rate for good office space in midtown Manhattan. *See id.*; Blackwell, *supra* note 1, at A1.

5. Blackwell, *supra* note 1, at A1.

out of the glitz and glamour of New York City came at a cost, however. In return, Virginia state and local governments provided millions of dollars of incentives and tax credits for Philip Morris's move. The Governor's Opportunity Fund[6] gave Philip Morris a $3 million grant, while the Virginia Investment Partnership Grant[7] supplied $25 million dollars paid in annual installments if the company met certain performance criteria.[8] In addition to the state grants, the City of Richmond offered $2 million in incentives, while Henrico County offered $1 million.[9] Philip Morris could also take advantage of a host of state and local tax credits designed to encourage economic development within the state.[10] Furthermore, state officials estimated the average salary of the 450 employees that Philip Morris planned to bring to Richmond at $133,000.[11] The Commonwealth traded millions of dollars of tax revenue and grants for an expansion of industry within the state and several high-paying jobs.

Philip Morris's move was one of many recent examples of corporations taking advantage of millions of dollars of grants, tax credits, and other monetary incentives that state and local governments have offered companies to expand or relocate within their borders.[12] In an increasingly competitive marketplace,

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6. To be eligible for the Fund, "projects must receive a minimum amount of private investment and create a minimum number of jobs, depending on the size of the locality in which the applicant business is located." Virginia Department of Business Assistance, Governor's Opportunity Fund, http://www.dba.state.va.us/financing/crd/program.asp?PROGRAM_ID=24 (last visited Mar. 31, 2006).

7. As with the Governor's Opportunity Fund, the governor has the final say over whether to authorize the grant. The grants are "paid in five equal annual installments, beginning in the fourth year after the capital investment and job creation are completed, or in the third year if the company is locating in a fiscally distressed area of the state." VIRGINIA ECONOMIC DEVELOPMENT PARTNERSHIP, A GUIDE TO BUSINESS INCENTIVES: 2005–2006, 17, *available at* http://www.yesvirginia.org/pdf/guides/4575-BusInc2005.pdf.

8. Blackwell, *supra* note 1, at A1.

9. *Id.* Officials also created a special enterprise zone to make Philip Morris eligible for incentives available in the state, such as tax credits through the Virginia Department of Housing and Community Development. *See* Pristin, *supra* note 4, at C5.

10. For a description of the tax incentives available on a statewide level in Virginia, see Virginia Economic Development Partnership, *supra* note 7, at 5–7.

11. Blackwell, *supra* note 1, at A1. Taken as a whole, officials estimated that the deal reached between Philip Morris and the Commonwealth could result in as many as 2000 new jobs. *See id.*

12. Last November, Nissan North America and Tennessee reached a deal that gave the carmaker $197 million in state and local tax incentives for moving from California to the Volunteer state. The package was so large and out of the ordinary that the state enacted special legislation to make it happen. For example, Nissan will be the recipient of new tax credits aimed at compensating the company for its moving expenses. *See* Bush

states have sought to increase their arsenal of options available to induce companies into expanding or staying at home. While the range of incentives offered may vary from locality to locality, nearly all states offer some type of incentives for economic investment.[13] As Professor Walter Hellerstein, the nation's preeminent scholar in the field of constitutional limitations on state taxation, noted, "[s]carcely a day passes without some state offering yet another incentive to spur economic development."[14] Although tax incentives have become commonplace in the world of economic development, the policy of offering companies tax breaks and credits is not without its critics. The criticism launched at economic incentives, specifically tax breaks, is primarily two-fold: economic and legal.

Critics of tax incentives argue that there are a host of reasons why the pervasive use of such incentives is a fiscally unsound practice. One complaint is that the current system allows public officials to unfairly pick and choose which companies and projects will receive millions of dollars of aid.[15] Others argue that such tax breaks allow states to relinquish millions of dollars of corporate tax revenue that could be spent to both improve the lives of state residents and improve a state's ability to compete in the marketplace.[16] Perhaps the most basic criticism of the broad use of tax

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Bernard, *Nissan Deal New Benchmark, Economic Developers Say*, THE TENNESSEAN, Dec. 4, 2005, at 3A.

13. According to one estimate made in February 2005, nearly forty states offered such incentives. *See* Bill King, *The War Against Incentives Rages On*, Expansion Management Online (Feb. 14, 2005), *available at* http://www.expansionmanagement.com/smo/articleviewer/default.asp?cmd=articledetail&articleid=16353&st=2. However, this figure is likely a conservative one since it is increasingly seen as bad policy not to offer businesses tax incentives to relocate or expand business within one's state.

14. Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 790 (1996).

15. For example, in Virginia, where the governor can exercise discretion over which companies or projects can receive financial aid out of the Governor's Opportunity Fund and the Virginia Investment Partnership Grant, supporters of a new baseball stadium for the Richmond Braves, the city's minor league baseball team, questioned why state and local officials balked at the opportunity to offer tax incentives to help build a new home for the team while those same officials aggressively wooed NASCAR with a multimillion dollar incentive package to make Richmond the home of the racing league's hall of fame. *See* Scott Bass, *Illegal Bait? The Latest in Business Lures: Tax Incentives may be Unconstitutional*, STYLE WKLY., Aug. 31, 2005, *available at* http://www.styleweekly.com/article.asp?idarticle=10880. Ultimately, Richmond was not selected for the hall of fame site. *See* Greg Engle, *NASCAR Narrows it Down*, SCRIPPS HOWARD NEWS SERVICE, Jan. 6, 2006.

16. *See* MICHAEL MAZEROV, CENTER ON BUDGET & POLICY PRIORITIES, SHOULD CONGRESS AUTHORIZE STATES TO CONTINUE GIVING TAX BREAKS TO BUSINESSES? 2 (2005), *available at* http://www.cbpp.org/2-18-05sfp.pdf ("[T]he loss of revenue is impairing the

incentives is that they are not nearly as vital to the creation of jobs and growth of business as proponents of tax incentives believe.[17] Opponents of tax incentives claim that "no business executive worth his salt will make a location decision based on state tax incentives."[18] They claim that other factors, such as an educated workforce, geographic location,[19] and transportation infrastructure are equally or more important than tax incentives in business decision-making.[20] Regardless of the effectiveness of tax

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ability of states to fund education, infrastructure improvements, worker retraining, and other public services that make a vital contribution to healthy state economies and a productive national economy.").

17. In his analysis of the research conducted examining the relationship between state taxes, incentives, and their effect on economic development, Robert G. Lynch found that

> the evidence fails to support the claim that growing the economy requires shrinking the public sector and reducing taxes. In particular, there is little evidence that state and local tax cuts—when paid for by reducing public services—stimulate economic activity or create jobs. There is evidence, however, that increases in taxes, when used to expand the quantity and quality of public services, can promote economic development and employment growth.

ROBERT G. LYNCH, RETHINKING GROWTH STRATEGIES: HOW STATE AND LOCAL TAXES AND SERVICES AFFECT ECONOMIC DEVELOPMENT, at vii (2004), *available at* http://www.epinet.org/books/rethinking_growth_(full).pdf.

18. David Brunori, *The Politics of State Taxation: Helping States to Hurt Themselves*, STATE TAX TODAY, June 6, 2005, *available at* 2005 STT 107-5 (LEXIS).

19. In its pitch for the NASCAR Hall of Fame, Henrico County officials touted Richmond's geographic location as one of the most important reasons to build the shrine there. According to a press release issued by Henrico County, "[m]ore than 50% of the U.S. population is within a one-day drive of Richmond and the area has an excellent, easy-to-navigate highway system and an international airport. Major attractions 100 miles away or less include Washington D.C., Virginia Beach, Williamsburg and the Blue Ridge Mountains." Press Release, Henrico County Submits Letter of Intent for Richmond Area to Land NASCAR Hall of Fame, *available at* http://www.rir.com/news/news.jsp?news_id=151.

In the end, NASCAR selected the city of Charlotte, North Carolina, as the site of its Hall of Fame. The Hall of Fame will cost Mecklenburg County approximately $107 million. Of that amount, $102 million will be raised though an increase in the local hotel tax. *See* Bob Rayner and John Markon, *Why City Lost 1 Bid but Won Another; In Seeking NASCAR Hall, MeadWestvaco, Long-Term Ties Crucial*, RICH. TIMES-DISPATCH, Mar. 12, 2006, at B1. After losing the race for the NASCAR Hall of Fame, the city bounced back with the announcement that MeadWestvaco, a Fortune 500 packaging company, would relocate from Connecticut to Richmond. *Id.* ("The state promised $6 million in incentive grants, based on the company meeting investment and employment goals. It also offered job training that could cost about $700,000. To put those incentives in perspective, MeadWestvaco has a market value of about $4.8 billion. The state incentives are worth about one-seventh of 1 percent of the company's total value.").

20. In light of the anti-smoking climate created by New York City's fiscal and social policies, it was no surprise that Philip Morris chose to leave Manhattan, regardless of how much the company claimed that a move to Virginia was too financially appealing to pass up. At the time the company announced its move, New York and Virginia had drastically different taxes on cigarettes: New York's tax climbed to $1.50 per pack while Virginia's tax remained the lowest in the nation at 2.5 *cents* per pack. Blackwell, *supra* note 1, at A1. Commentators also believe the company was blowing smoke when it denied that New

incentives or the questionable role they play in business decision-making, tax incentives have proliferated across the nation. In this age of outsourcing, politicians face immense pressure to keep jobs at home, and when new jobs are created, they are quick to associate themselves with job growth. Therefore, it can be expected that politicians and the state tax analysts who work for them are resistant to limiting incentives or any other tools that may help their state compete for jobs with other states. Unsurprisingly, opponents of tax incentives have been unsuccessful, thus far, in convincing state legislatures to forego these tax credits.

Finding their arguments to be unpopular in statehouses across the country, opponents of tax incentives have taken their battle to the courts. In recent years, lower courts have wrestled with questions about the constitutionality of several economic incentives.[21] This battle has now reached the Supreme Court, which heard oral arguments for *DaimlerChrysler Corp. v. Cuno*[22] on March 1, 2006.[23] In *Cuno*, the Supreme Court will consider whether the

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York City's smoking ban, one that forbids Philip Morris employees from lighting up in their offices, played any role in its decision to leave Manhattan. *See, e.g.*, Nancy Dillon, *Philip Morris to Quit City: Mayor's Smoking Ban Seen Behind Va. Move*, N.Y. DAILY NEWS, Mar. 4, 2003, at 27.

21. *See, e.g.*, Pelican Chapter, Associated Builders and Contractors, Inc. v. Edwards, 128 F.3d 910 (5th Cir. 1997) (holding that Louisiana property tax exemption for a new, or addition to an existing, manufacturing establishment violated the dormant Commerce Clause because eligibility for the exemption required manufacturers and contractors to employ eighty percent in-state workers and use eighty percent in-state materials); GMC v. Dir. of Revenue, 981 S.W.2d 561 (Mo. 1998) (holding that Missouri law that allowed companies and their subsidiaries to file consolidated income tax returns only if fifty percent or more of its income had come from sources within Missouri violated the Commerce Clause); Worldcorp v. Dep't of Taxation, 944 P.2d 824 (Nev. 1997) (striking down a statute that gave air carriers headquartered in Nevada a sales and use tax exemption on its aircrafts while denying the same for corporations headquartered outside of the state).

22. 126 S. Ct. 36 (2005).

23. In granting certiorari, the Supreme Court asked the parties to present briefs for an additional question: "Whether respondents have standing to challenge Ohio's investment tax credit, OHIO REV. CODE ANN. § 5733.33." *Id.* Because *Cuno* involves several parties, individuals and businesses, from two different states, the issue of standing is multifaceted. However, when adding into the equation that the respondents are taxpayers, the standing question becomes even more complex. The circuits are split over the standard to apply for grievances filed by state taxpayers against state laws in federal court. *See* Kristin E. Hickman, *How Did We Get Here Anyway? Considering the Standing Question in* DaimlerChrysler v. Cuno, 4 GEO. J.L. & PUB. POL'Y 4 (forthcoming 2006), *available at* http://ssrn.com/abstract=859784 (last visited Mar. 31, 2006). According to Professor Kristin E. Hickman, the standing issue in *Cuno* comes down to whether the Supreme Court believes that "states should be treated more like the federal government or like municipalities in evaluating taxpayer standing." *Id.* Hickman predicts that the Supreme Court will rule against the plaintiff taxpayers in *Cuno* under a standing analysis, ignoring the Commerce Clause issue altogether. *Id.* at 30. For an analysis of the impact this result would have on

State of Ohio's Manufacturing Machinery & Equipment Investment Tax Credit ("investment tax credit" or "ITC"), which gives a credit against a corporation's franchise or income tax depending upon where the taxpayer installs new machinery in the state and the size of the investment, violates the dormant Commerce Clause.[24] The Court of Appeals for the Sixth Circuit invalidated the investment tax credit because it discriminated against interstate commerce in violation of the dormant Commerce Clause.[25] The potential impact of this case goes well beyond the cities of Toledo and Richmond.[26] The Sixth Circuit's decision sent notice to the thirty-seven states that offer similar credits that their tax incentives might now be in legal jeopardy.[27] *DaimlerChrysler Corp. v. Cuno*, which started out as a challenge against a state tax credit, is now a case of national importance.

This comment examines *Cuno* and the impact the case may have on the use of tax incentives under the dormant Commerce

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this sort of litigation, see discussion *infra* Part VI.

If oral arguments serve as any indicator of the Court's position on an issue, the oral arguments in *Cuno* would suggest that Professor Hickman might be correct. The Justices spent a considerable amount of time grilling both parties on the question of standing. *See generally* Transcript of Oral Argument at 4–15, 27–36, *Cuno*, 126 S. Ct. 36 (No. 04-1704), *available at* http://www.supremecourtus.gov/oral_arguments/argument_transcripts/04-1704.pdf [hereinafter Transcript of Oral Argument].

24. In lower courts, the cases were known as *Cuno v. DaimlerChrysler, Inc.* and *Cuno v. Wilkins*. Here, the petitioner, William W. Wilkins, is Ohio's Tax Commissioner. The two cases were consolidated. The question presented is "[w]hether Ohio's investment tax credit, Ohio Revised Code § 5733.33, which seeks to encourage economic development by providing a credit to taxpayers who install new manufacturing machinery and equipment in the State, violates the Commerce Clause of the United States Constitution." DaimlerChrysler Corp. v. Cuno, No. 04-1704, question presented (U.S. Sept. 27, 2005), *available at* http://www.supremecourtus.gov/qp/04-01724qp.pdf.

25. *See* Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 746 (6th Cir. 2004).

26. While companies that move to Richmond or expand their business in the city have several tax incentives to choose from, it is important to note that the bulk of the Philip Morris package was funded through grants, which is discussed in Part IV, are currently constitutional. *See* discussion *infra* Part IV. The Virginia Enterprise Zone Program reported that one business qualified for the state's investment tax credit in 2004. Since 2000, two businesses have received $3.04 million in investment tax credits while making $1.38 billion in capital improvements and equipment expenditures and creating 2085 full time jobs. VA. ENTERPRISE ZONE PROGRAM, VA. DEP'T OF HOUSING AND COMMUNITY DEVELOPMENT, 2004 TAX YEAR ANNUAL REPORT 10 (2004), *available at* http://www.dhcd.virginia.gov/EZones/docs/2004_EZone_Program_Report.pdf.

27. Thirty-seven states base their investment tax credits upon capital investment and/or job creation in the state. *See, e.g.*, ALA. CODE § 41-23-24 (LexisNexis 2000); CAL. REV. & TAX. CODE § 23649 (West 2004); FLA. STAT. ANN. § 220.191 (West 2005); 35 ILL. COMP. STAT. 5/201(f) (2005); MD. ANN. CODE art. 83a, § 5-1501 (2003); N.C. GEN. STAT. § 105-129.9 (2005); N.Y. TAX LAW § 210(12)(a) (Consol. 1990); VA. CODE ANN. § 59.1-280.1 (2001).

Clause. Part II examines the Ohio Investment Tax Credit and the facts that gave rise to the controversy in *Cuno*. Part III analyzes the Supreme Court's relevant jurisprudence in the area of tax incentives and the dormant Commerce Clause. Part IV reviews the Sixth Circuit's opinion in *Cuno* and analyzes whether the court correctly followed Supreme Court precedent. Finally, Part V assesses the ramifications on the dormant Commerce Clause and tax incentives of a Supreme Court decision upholding or reversing the Sixth Circuit.

II. THE OHIO INVESTMENT TAX CREDIT

In the summer of 1995, fearing a downturn in the economy, the Ohio legislature hurried a bill through both of its chambers that would encourage businesses to remain in the state by giving them a tax credit for the purchase of new equipment and machinery.[28] In under a month after Senate Bill 188 was introduced, Governor George Voinovich put the act into effect with his signature.[29] The move was seen as saving thousands of jobs and was widely praised throughout the state.[30] The investment tax credit works as a nonrefundable credit against the state's corporate franchise tax[31] if the taxpayer "purchases new manufacturing machinery and equipment during the qualifying period . . . [and] the new manufacturing machinery and equipment are installed in [Ohio]."[32] The investment tax credit is 13.5% of the cost of the new investment if it is purchased for use in "eligible areas" of the county.[33] Eligible areas include those designated as a "distressed area, a labor surplus area, an inner city area, or a situational distress area."[34] Otherwise, similar investments made in non-eligible areas could receive an ITC of 7.5%.[35] According to the Ohio De-

28. *See* Lee Leonard, *Tax Credit Proposal is Sent to House After Senate's Approval*, COLUMBUS DISPATCH, July 1, 1995, at 3C. Only four Ohio state senators voted against the bill. *Id.* Interestingly, Toledo's representative was one of the four. *See id.*

29. *See* S.B. 188, 121st Gen. Assem., Reg. Sess. (Ohio 1995).

30. *See* Editorial, *Ohio Competes; Tax Credit is a Wise Investment in Jobs*, COLUMBUS DISPATCH, July 26, 1995, at 10A.

31. *See* OHIO REV. CODE ANN. § 5733.01 (LexisNexis 2005).

32. *Id.* § 5733.33(B)(1) (LexisNexis 2005).

33. *Id.* § 5733.33 (C)(2) (LexisNexis 2005).

34. *Id.* § 5733.33(A)(9) (LexisNexis 2005). For an explanation of what constitutes each type of eligible area, see *id.* § 5733.33(A)(8)-(13) (LexisNexis 2005).

35. *See id.* § 5733.33(C)(1) (LexisNexis 2005).

partment of Taxation, there were 2312 claims for the investment tax credit in 2004, valued at $86.9 million.[36] The Ohio Department of Development estimates that there have been more than 18,000 filings for the ITC since the credit was created in 1995.[37] Figures from the Department of Development show that companies in Ohio have invested $34.2 billion in new machinery and equipment, making them eligible for more than $2 billion in tax credits.[38] When the tax credit was introduced, opponents of the ITC argued that giving away $300 million over thirteen years was too large a sacrifice,[39] and it is clear that the credit has already exceeded those estimates.

In July 1997, the Chrysler Corporation announced that it planned on spending nearly $1.2 billion to build a Jeep assembly plant and revamp an existing factory in Toledo, Ohio.[40] Chrysler considered leaving the industrial city for another location and taking its 5500 employees with it.[41] Under considerable pressure from Toledo residents[42] and facing competition from bordering Michigan, city and state officials offered Chrysler an estimated $232 million incentive package to stay in Toledo.[43] Millions of dollars of tax revenue was not the only thing that Toledo and its residents gave up in the deal. When DaimlerChrysler[44] and the City of Toledo finalized their agreement in 1998, officials esti-

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36. OHIO DEP'T OF TAXATION, *Tax Data Series: Corporation Franchise Tax* (2005), *available at* http://tax.ohio.gov/divisions/tax_analysis/tax_data_series/corporation_franchise/cfcredit/documents/cf-creditsty04.pdf.

37. *Economic Development and the Dormant Commerce Clause: The Lessons of* Cuno v. DaimlerChrysler *and its Effect on State Taxation Affecting Interstate Commerce: Joint Hearing Before the Subcomm. on the Constitution of the H. Comm. on the Judiciary*, 109th Cong. 6 (2005) [hereinafter *Hearing*] (statement of the Honorable Bruce Johnson, Lieutenant Governor of Ohio).

38. *Id.*

39. *See* Editorial, *supra* note 30, at 10A.

40. Robyn Meredith, *Chrysler Wins Incentives From Toledo*, N.Y. TIMES, Aug. 12, 1997, at D3.

41. *See id.* While the city's incentive package persuaded the company to stay, Chrysler announced that the new plant would only require the employ of 4900 people. *See id.*

42. Perhaps no city official was more dedicated to seeing Chrysler stay than Toledo Mayor Carty Finkbeiner: "'Had we lost Jeep, it would be like Detroit losing the Tigers. It would be like the Yankees leaving New York,' Finkbeiner said. 'We don't have a major-league sports team. Jeep is a major part of our identity.'" John Seewer, *Jeep Runs Over Toledo Homes Neighborhood*, AKRON BEACON J., May 24, 1999, at B5.

43. Meredith, *supra* note 40, at D3.

44. The Chrysler Corporation and Daimler-Benz merged in the summer of 1998. *See* Ted Evanoff, *Chrysler Will Merge with Daimler-Benz; Move Likely Means Prestige, Greater European Sales for U.S. Automaker*, DETROIT FREE PRESS, May 7, 1998, at 1A.

mated that the incentive package was worth $280 million,[45] nearly $50 million more than initially expected. In the agreement, Toledo and two local school districts would give DaimlerChrysler a ten-year, one-hundred percent property tax exemption and an investment tax credit of 13.5% "against the state corporate franchise tax for certain qualifying investments."[46] To build the new plant, DaimlerChrysler needed land occupied by eighty-three homeowners and sixteen businesses in a Toledo neighborhood.[47] While some property owners left willingly, the city was forced to initiate eminent domain proceedings against the other owners to condemn their property.[48] This grabbed the attention of

45. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 741 (6th Cir. 2004).

46. *Id.*

47. Lisa Brennan, *Toledo 'Taken' With Jeep Suit*, THE NAT'L L.J., Jan. 25, 1999, at A1.

48. *Id.* Although controversial, exercising the Fifth Amendment's power of eminent domain to promote economic development was a common practice when Chrysler and Toledo reached their deal. *See* Steven E. Buckingham, *The* Kelo *Threshold: Private Property and Public Use Reinstated*, 39 U. RICH. L. REV. 1279, 1293–1305 (2005). Last year, in *Kelo v. City of New London*, 125 S. Ct. 2655 (2005), the Supreme Court heard a lawsuit brought by nine property owners against the city of New London, Connecticut to stop the condemnation of their homes, which was required by the city's development plan aimed at creating jobs and increasing tax revenue. *Id.* at 2658–60. The Court considered the question of whether taking private land to promote economic development was a public use under the Fifth Amendment. *Id.* at 2661. The Court answered:

> the necessity and wisdom of using eminent domain to promote economic development are certainly matters of legitimate public debate. This Court's authority, however, extends only to determining whether the City's proposed condemnations are for a "public use" within the meaning of the Fifth Amendment to the Federal Constitution. Because over a century of our case law interpreting that provision dictates an affirmative answer to that question, we may not grant petitioners the relief that they seek.

Id. at 2668. Although the power to tax and the power to take involve two different provisions of the Constitution, *Kelo* and the fight against tax incentives involve one fundamental question—how far can a state go in the name of economic development?

The *Kelo* decision created an uproar in communities and legislative chambers across America. In November, the House of Representatives, by a margin of 376 to 38, passed a bill that would forbid state officials from using federal funds to pay for economic development projects if eminent domain was involved. *See* Private Property Rights Protection Act, H.R. 4128, 109th Cong. (2005). Also, this year, it is expected that nearly half of state legislatures will debate new laws designed to curb *Kelo*. *See* Jennifer Bradley, *Property Wrongs; In Kelo's Wake, a Raft of Anti-Regulatory Initiatives from the Right*, THE AM. PROSPECT, Jan. 2006, at 16. Some opponents of tax incentives have tried to harness the *Kelo* backlash to support their cause, arguing that tax incentive packages like the one offered by Toledo have essentially the same detrimental effect on communities that takings do. *See, e.g.*, Robert D. Plattner, *New London and Its Aftermath: A Lesson for State Tax Policymakers*, STATE TAX TODAY, Aug. 29, 2005, at 679, *available at* 2005 STT 166-7 (LEXIS) ("In the name of economic development, the states are using tax policy to intrude in their economies as never before, violating basic principles of the free market and tax policy and too often granting favorable tax treatment to those with power and influence at the expense of the general welfare. The best that can be said for those tax policies is that

consumer advocate Ralph Nader, who helped angry Toledo taxpayers file a lawsuit against the plan in December 1999.[49] A group of eighteen plaintiffs from Ohio and Michigan filed suit in state court against the City of Toledo, the State of Ohio, the two school districts involved in the agreement, and several government officials.[50] The plaintiffs alleged that the property tax exemption and the investment tax credit violated the Commerce Clause of the United States Constitution and the Equal Protection Clause of the Ohio Constitution.[51] The defendants removed the case to federal court and filed a motion to dismiss.[52] The district court held that there were no violations of the Equal Protection Clause of the Ohio Constitution[53] and dismissed the remaining counts of the complaint alleging violation of the Commerce Clause.[54] The plaintiffs appealed the dismissal to the United States Court of Appeals for the Sixth Circuit.

III. THE DORMANT COMMERCE CLAUSE AND SUPREME COURT PRECEDENT

A. *The Dormant Commerce Clause*

Before reviewing the Sixth Circuit's opinion, it is necessary to analyze the Supreme Court's jurisprudence in the area of discrimination and the dormant Commerce Clause, a field of law that has been, perhaps justifiably, described as a "mess"[55] and a "quagmire."[56] The Commerce Clause of the Constitution states

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people don't lose their homes as a consequence. That is hardly justification for their continuation, however.").

49. *See* Lisa Brennan, *Toledo Tax Breaks Battled*, THE NAT'L L.J., Dec. 20, 1999, at A6.

50. The Michigan plaintiffs argued that had the tax incentives not been available, DaimlerChrysler would have built its new facilities in Michigan, giving Michigan, its municipalities, and its residents the tax revenue and job growth that would have been created with the new Jeep plant. *See* Hickman, *supra* note 23, at 6.

51. Cuno v. DaimlerChrysler, Inc., 154 F. Supp. 2d 1196, 1198 (N.D. Ohio 2001).

52. *Id.*

53. *Id.* at 1201–02. The district court found that the Equal Protection Clause was satisfied since there was a "rational nexus" between the exemption and credit and the legitimate state interest "to encourage industrial investment and development in Ohio." *Id.*

54. *Id.* at 1203–04. The merits of the plaintiffs' Commerce Clause argument will be addressed in Part IV's review of the Sixth Circuit's opinion. *See* discussion *infra* Part IV.

55. *Hearing*, *supra* note 37, at 15 (statement of Professor Walter Hellerstein).

56. Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 458 (1959).

that Congress shall have the power "[t]o regulate Commerce . . . among the several States."[57] Although nowhere stated in the Constitution, the doctrine, which proposes that a negative, or dormant, aspect of the Commerce Clause gives the judiciary the ability to review state economic regulation, began to develop as early as the Marshall and Taney Courts.[58] *Gibbons v. Ogden* is seen as the original dormant Commerce Clause case, but it was in the landmark decisions of *Case of the State Freight Tax*[59] and *State Tax on Railway Gross Receipts*[60] that the Court "unequivocally announced and squarely applied the doctrine that the Commerce Clause by its own force limits state tax power over interstate commerce."[61] While these decisions affirmed that the Court was willing to invalidate state tax laws that discriminated against interstate commerce, some state taxes on interstate commerce remained constitutional.[62] For the next one hundred years, the Supreme Court tussled with different standards of review and tests in cases that involved challenges to state tax policies.[63]

In 1977, the Supreme Court handed down its decision in *Complete Auto Transit, Inc. v. Brady*,[64] which provided a four-prong test to determine the validity, under the Commerce Clause, of a tax on interstate commerce.[65] In *Complete Auto Transit*, the Court assessed whether a Mississippi tax on an out-of-state manufacturer's automobiles for the "privilege of . . . doing business" within the state violated the Commerce Clause.[66] The *Complete Auto Transit* test asks four questions: (1) Does the tax apply to an activity that has a substantial nexus with the state?; (2) Is the tax fairly apportioned to activities conducted by the taxpayer in the state?; (3) Does the tax discriminate against interstate com-

57. U.S. CONST. art. I, § 8, cl. 3.

58. *See* WALTER HELLERSTEIN, TAX MANAGEMENT MULTISTATE TAX PORTFOLIOS, FEDERAL CONSTITUTIONAL LIMITATIONS ON STATE TAXATION, 1400:0005-:0009 (2005).

59. 82 U.S. (15 Wall.) 232, 232, 282 (1872) (holding that a Pennsylvania tax imposed on freight carried in the state was a regulation of commerce national in nature and therefore unconstitutional).

60. 82 U.S. (15 Wall.) 284 (1872) (holding that a Pennsylvania tax on freight receipts did not violate the Commerce Clause because it was not a tax on the freight but on the property held by a corporation).

61. HELLERSTEIN, *supra* note 58, at 1400:0006.

62. *See id.* at 1400:0005-:0008.

63. *See id.* at 1400:0005-:0010.

64. 430 U.S. 274 (1977).

65. *See id.* at 277–78.

66. *Id.* at 274.

merce?; and (4) Is the tax fairly related to services provided by the state?[67]

While all of the prongs of the *Complete Auto Transit* test are important and interrelated, the prong that asks whether the tax discriminates against interstate commerce is critical to the resolution of cases like *Cuno*. Prior to *Cuno*, the Supreme Court had several opportunities to review state tax provisions to determine the bounds of nondiscrimination. The cases below define the Court's position on state tax incentives and the dormant Commerce Clause.

B. *Supreme Court Precedent*

1. The *Boston Stock Exchange* Case

In *Boston Stock Exchange v. State Tax Commission*,[68] the Supreme Court considered whether an amendment to New York's tax on securities transactions was constitutional.[69] In 1968, the New York legislature responded to increased competition from regional stock exchanges in places like Los Angeles and Chicago by increasing the tax rate on securities transactions involving out-of-state sales.[70] Since 1905, New York utilized a levy—a transfer tax—on securities transactions if part of the transaction happened within the state.[71] Moreover, the states in which the petitioners, competing stock exchanges, were located did not tax the sale or transfer of securities.[72] New York tweaked the transfer tax so that transactions, delivery or transfer of security sale, occurring in-state, had a lower tax burden than those occurring out-of-state.[73] Specifically, if a nonresident wanted to sell a security

67. *Id.* at 277–78. For background on the application of the *Complete Auto Transit* test, see HELLERSTEIN, *supra* note 58, at 1400:0010-:0022a.

68. 429 U.S. 318 (1977).

69. *Id.* at 319.

70. *Id.* Competition from the other exchanges increased by seventy-three percent in the two years before the New York transfer tax was amended. *Id.* at 325 n.7.

71. *Id.* at 319. New York recognized that improvements in technology, especially in the area of communication, aided the establishment of regional stock exchanges. New York had a near monopoly on stock transfers, but these improvements in technology meant that it would be easier for investors scattered across the nation to use regional stock exchanges rather than rely on the New York Stock Exchange. *See id.* at 328 n.10.

72. *Id.* at 323.

73. *Id.* at 324.

on the New York Stock Exchange, he would get a fifty percent decrease on the tax rate with a $350 maximum tax liability for a single transaction.[74] On the other hand, if the nonresident opted to sell on an out-of-state exchange, a higher transfer tax applied and there was no limitation on total tax liability.[75] Finding that residents increasingly used out-of-state exchanges, the amendment was structured to encourage residents to use the New York Stock Exchange, "foreclos[ing] tax-neutral decisions."[76]

A unanimous Supreme Court held that the amended transfer tax discriminated against interstate commerce because the "obvious effect of the tax is to extend a financial advantage to sales on the New York exchanges at the expense of regional exchanges."[77] The Court restated its position that "[a] State may no more use discriminatory taxes to assure that nonresidents direct their commerce to businesses within the State than to assure that residents trade only in intrastate commerce."[78] While striking down a state tax aimed at promoting the New York economy, the Court noted that its decision "does not prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry."[79] *Boston Exchange* provided the states with an example of an impermissible tax, but the Court did not provide them with any additional guidance on how to structure constitutional tax credits.[80]

2. The *Westinghouse Electric Corporation* Case

Westinghouse Electric Corp. v. Tully[81] presented the Supreme Court with another question concerning the constitutionality of an income tax credit. The New York legislature enacted a tax credit in response to the changes Congress made to the Internal

74. 429 U.S. at 324.
75. *Id.* at 324–25.
76. *Id.* at 331.
77. *Id.*
78. *Id.* at 334–35.
79. *Id.* at 336.
80. Walter Hellerstein commented that *Boston Exchange*—despite its pronouncement that some taxes could be arranged to encourage economic development—left open to interpretation the concept that *all* tax incentives were unconstitutional since a business offered the incentive would not consider only non-tax criteria in a business decision. Hellerstein & Coenen, *supra* note 14, at 795–96.
81. 466 U.S. 388, 389 (1984).

Revenue Code when it passed the Revenue Act of 1971.[82] In that bill, Congress created a special corporate entity called the "Domestic International Sales Corporation" or "DISC."[83] Congress amended the Code in order to aid American firms in increasing their exports by providing them with tax incentives.[84] Since the measure precluded a DISC's income from being taxed, New York, which ordinarily would have incorporated the DISC tax scheme into its laws, would have lost between $20–$30 million annually in tax revenue if it followed the federal scheme.[85] There was fear that taxing DISCs would both discourage the companies from forming in New York and also suppress the production of export goods within the state.[86] The New York legislature drafted legislation that was designed to achieve two things: (1) consolidate the income of the DISC with the income of its parent for state tax purposes and; (2) provide a partial franchise tax credit to the parent company by lowering the tax rate to thirty percent on DISC income as reflected in consolidated return.[87] However, the maximum credit was adjusted according to the ratio of exports the DISC shipped from New York compared to the number shipped from outside the state.[88] Thus, the more business activity the DISC conducted in-state, the greater the incentive it would recognize from the State of New York.

Westinghouse Electric Corporation, a Pennsylvania corporation that conducted business in New York, was the parent company of Westinghouse Electric Export, which generated revenue entirely from export sales.[89] In 1973, Westinghouse Electric's tax report did not include all of its DISC's income on its consolidated tax returns.[90] Westinghouse Electric and the New York Tax Commission disputed over the correct tax determination, and when the disagreement could not be resolved through administrative appeals, Westinghouse Electric brought suit, claiming that "the tax benefit of the DISC export credit to gross receipts from shipments

82. *Id.* at 390.
83. *Id.*
84. *See id.*
85. *Id.* at 392. In New York, a subsidiary company is taxed directly, not on its distributions received by a parent from the subsidiary. *Id.*
86. 429 U.S. at 392–93.
87. *Id.* at 393.
88. *Id.*
89. *Id.* at 394.
90. *Id.* at 395.

attributable to a New York place of business violated the Commerce, Due Process, and Equal Protection Clauses."[91]

A unanimous Supreme Court agreed with Westinghouse Electric. Although the Court agreed with the New York Tax Commission that the state's allocation formula was constitutional, it held that the tax credit scheme violated the Commerce Clause because it gave an incentive to a company to conduct more business in the state while it "penalize[d] increases in the DISC's shipping activities in other States."[92] The Court reaffirmed the central tenet of *Boston Exchange* that a tax is discriminatory when it "diverts new business into the State or merely prevents current business from being diverted elsewhere."[93] Though it struck down another tax credit that was created to promote economic activity within a state, the Supreme Court maintained once again that states were free to compete among themselves for business, but doing so at the cost of discriminating against interstate commerce was antithetical to the Commerce Clause's position against protectionism.[94]

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91. 429 U.S. at 395–96.

92. *Id.* at 400–01.

93. *Id.* at 406.

94. *See id.* at 406 n.12. Later that year, the Supreme Court held that a Hawaiian tax exemption violated the Commerce Clause because it saved certain Hawaii-produced liquors from the twenty percent excise tax that applied to other liquors made outside the state. The Supreme Court found the exemption unconstitutional for the same reasons that it found the credits in *Boston Stock Exchange* and *Westinghouse* infirm—the measure had the purpose and effect of discriminating in favor of local products over out-of-state ones. *See* Bacchus Imps., Ltd. v. Dias, 468 U.S. 263, 265, 273 (1984).

Unlike *Boston Stock Exchange* and *Westinghouse*, however, the decision was far from unanimous. Justices Stevens, Rehnquist, and O'Connor dissented, arguing that the Twenty-First Amendment precluded the Court from striking down the tax exemption. *Id.* at 287 (Stevens, J., dissenting). According to the dissenters, Supreme Court jurisprudence established that the Twenty-First Amendment "confers power upon the States to regulate commerce in intoxicating liquors unconfined by ordinary limitations imposed on state regulation of interstate goods by the Commerce Clause and other constitutional provisions." *Id.* at 281 (Stevens, J., dissenting).

Last year, the Supreme Court reexamined the constitutional conflict between the Commerce Clause and the Twenty-First Amendment. In *Granholm v. Heald*, 125 S. Ct. 1885 (2005), the Supreme Court considered a challenge to New York and Michigan state laws that allowed their residents to directly purchase wine from in-state wineries while requiring out-of-state wineries to sell through an in-state wholesaler before their products could reach consumers. *Id.* at 1891–92. In a five-to-four decision, the Court again held that the Commerce Clause trumped the Twenty-First Amendment. *Id.* at 1907. With Justice Thomas, writing one of the case's two dissents, Justices O'Connor, Stevens, and Rehnquist renewed their argument that the Twenty-First Amendment and the Webb-Kenyon Act barred the application of the Commerce Clause. *See id.* at 1910 (Thomas, J., dissenting).

Allowing States to regulate the direct shipment of liquor was of "clear con-

3. The *New Energy Company* Case

Before *Cuno*, the Supreme Court's most recent challenge to a state tax credit came in *New Energy Company of Indiana v. Limbach*.[95] In *New Energy*, the Supreme Court reviewed a provision in the Ohio code that gave fuel dealers a tax credit for each gallon of ethanol sold against the state's motor fuel sales tax if that ethanol was produced in Ohio or in another state that gave an incentive to Ohio-produced ethanol.[96] An Indiana ethanol manufacturer brought suit against the state because it was not eligible for the reciprocity following Indiana's switch from a tax exemption for ethanol to a direct subsidy.[97] Ohio argued that its policy was not discriminatory but one that encouraged other states to enact similar legislation.[98] Although the Court stated that "reciprocity requirements are not *per se* unlawful,"[99] the Court, in a unanimous decision, struck down the tax credit, stating that "the threat used to induce Indiana's acceptance is, in effect, taxing a product made by its manufacturers at a rate higher than the same product made by Ohio manufacturers."[100]

Furthermore, the Court settled the contention that a "[s]tate may validate a statute that discriminates against interstate commerce by showing that it advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives."[101] The Supreme Court stated that "the stan-

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> cern" to the framers of the Webb-Kenyon Act and the Twenty-first Amendment. The driving force behind the passage of the Webb-Kenyon Act was a desire to reverse this Court's decisions that had precluded States from regulating the direct shipment of liquor by out-of-state interests. . . . [T]here is little evidence that purely protectionist tax exemptions like those at issue in *Bacchus* were of any concern to the framers of the Act and the Amendment.

Id. at 1924–25 (Thomas, J., dissenting) (internal citations omitted).

95. 486 U.S. 269 (1988).

96. *Id.* at 271.

97. *Id.* at 272–73. Although not addressing the constitutionality of subsidies, the Court stated that "[d]irect subsidization of domestic industry does not ordinarily run afoul" of the dormant Commerce Clause. *Id.* at 278. For an examination of the treatment of subsidies under the dormant Commerce Clause, see discussion *infra* Part V.

98. 486 U.S. at 274.

99. *Id.* at 276 (citing Kane v. New Jersey, 242 U.S. 160 (1916) (holding that there was no violation of the Fourteenth Amendment where New Jersey Automobile Law treated its citizens differently than citizens from states who did not accept an offer of reciprocity)).

100. *Id.*

101. *Id.* at 278.

dards for such justification are high."[102] Ohio advanced two arguments as legitimate local purposes: (1) promoting ethanol, a component of gasohol, would reduce harmful exhaust emissions and; (2) providing a reciprocity condition would help persuade other states to provide incentives for ethanol production as well.[103] The Court held that each of Ohio's arguments were "no more than implausible speculation, which does not suffice to validate this plain discrimination against products of [an] out-of-state manufacture."[104] Theoretically, there may be a situation where the Court will uphold a discriminatory state statute or policy because of the unavailability of nondiscriminatory alternatives, but it seems very unlikely that such a situation will arise, especially with the powers that state and local governments already have to promote public health, safety, and welfare.

IV. *CUNO V. DAIMLERCHRYSLER*

A. *The Sixth Circuit Opinion*

The Sixth Circuit Court of Appeals reviewed *de novo* the lower court's order that dismissed the plaintiff's challenge to the Ohio ITC and personal property tax exemption.[105] The court did not review whether all prongs of the *Complete Auto Transit* test were satisfied because the parties only placed discrimination against interstate commerce at issue.[106] But the Sixth Circuit did thoroughly examine the Supreme Court's jurisprudence in the area. Although the Sixth Circuit surmised that the Court "has never precisely delineated the scope of the doctrine that bars discriminatory taxes,"[107] the court found that the dormant Commerce Clause "rests on the distinction between laws that benefit in-state activity and laws that burden out-of-state activity."[108] The State of Ohio's position was that the Supreme Court's cases meant that

102. *Id.*; *see also* Philadelphia v. New Jersey, 437 U.S. 617, 624 (1978) ("[W]here simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected.").

103. 486 U.S. at 279–80.

104. *Id.* at 280.

105. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 742 (6th Cir. 2004).

106. *See id.*

107. *Id.* at 743.

108. *Id.* at 745.

tax incentives were unconstitutional only if they either imposed a higher tax on out-of-state products or businesses or factored both a business's out-of-state and in-state activities to calculate the business's tax rate.[109] Under this broad but simple guideline, the Sixth Circuit rejected Ohio's argument that *Boston Stock Exchange* and its progeny should be "read narrowly to hold that tax incentives, like the Ohio tax credit, are permissible as long as they do not penalize out-of-state economic activity."[110] Ohio's ITC gave in-state companies the option of reducing their corporate tax by expanding their businesses in the state.[111] Conversely, in-state companies could not take advantage of the investment tax credit if they chose to expand outside of the state. Therefore, as the Sixth Circuit stated, the Ohio ITC violated the Commerce Clause because it coerced companies to conduct more business in the state.[112]

Although not at issue before the Supreme Court, it is necessary to review the Sixth Circuit's decision to uphold Ohio's personal property tax exemption in comparison to its invalidation of the Ohio ITC. Ohio code allows municipalities to offer certain incentives to a business that "agrees to establish, expand, renovate, or occupy a facility and hire new employees, or preserve employment opportunities for existing employees" in areas designated as economically depressed.[113] The *Cuno* plaintiffs argued that the tax exemption was discriminatory because taxpayers who did not want to locate within enterprise zones were treated less preferentially compared to taxpayers who did locate within such areas.[114] The Sixth Circuit held that the conditions the property tax exemption placed on a potential taxpayer may have been unconsti-

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109. *Id.*

110. *Id.* (citing Philip M. Tatarowicz & Rebecca F. Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 VAND. L. REV. 879, 929 (1986) ("[T]he key to finding a tax incentive unconstitutionally discriminatory appears to be a reliance by the state tax provision on both a taxpayer's in-state and out-of-state activities in determining the taxpayer's effective tax rate. Such a provision clearly has a negative impact on interstate commerce. A provision that relies exclusively on a taxpayer's in-state activities in determining an effective tax rate, however, arguably does not have a negative effect on interstate commerce.")). It is important to note that the authors of this analysis of the constitutionality of state tax incentives did not have the Supreme Court's opinion in *New Energy* to evaluate, a decision which bolstered rather than retreated from the core tenets of nondiscrimination and the Commerce Clause.

111. 386 F.3d at 741.

112. *See id.* at 746.

113. OHIO REV. CODE ANN. § 5709.62(C)(1) (LexisNexis 2005).

114. 386 F.3d at 746.

tutional independently, but the exemptions are not discriminatory if they do not require the taxpayer to "engage in another form of business in order to receive the benefit or [are] limited to businesses with a specified economic presence."[115]

The Sixth Circuit relied upon a recent Supreme Court case, *Camps Newfound/Owatonna, Inc. v. Town of Harrison*,[116] which called on the Court to decide "whether an otherwise generally applicable state property tax violates the Commerce Clause . . . because its exemption for property owned by charitable institutions excludes organizations operated principally for the benefit of nonresidents."[117] In that case, a Maine nonprofit corporation that ran a summer camp for children who follow Christian Science sued the Town of Harrison because it could not reap the benefit of the property tax exemption due to the fact that most of its campers were nonresidents.[118] In a 5-4 decision,[119] the Supreme Court held that the property tax exemption was unconstitutional because it "distinguishe[d] between entities that serve a principally interstate clientele and those that primarily serve an intrastate market, singling out camps that serve mostly in-staters for beneficial tax treatment, and penalizing those camps that do a principally interstate business."[120] Unlike those in place in the tax exemption of *Camps Newfound*, the conditions of Ohio's property tax exemption were "related to the use or location of the property itself" and therefore constitutional.[121]

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115. *Id.*

116. 520 U.S. 564 (1997).

117. *Id.* at 567.

118. *Id.* at 567–69.

119. Justice Stevens wrote for the majority, joined by Justices O'Connor, Kennedy, Souter, and Breyer. *Id.* at 566. Two dissents were filed. *Id.* Justice Thomas filed a dissent, *id.*, which will be discussed in Part V.A. Justice Scalia filed the second dissent, joined by Justices Rehnquist, Thomas, and Ginsburg. *Id.* Justice Scalia argued that the Court had read the dormant Commerce Clause too broadly. *See id.* at 595–96 (Scalia, J., dissenting). Scalia suggests that there may be a need to form other exceptions to the dormant Commerce Clause other than "market participant" or "subsidy" exceptions. *Id.* at 608 (Scalia, J., dissenting). According to Justice Scalia, Maine's tax exemption policy "has nothing to do with economic protectionism" and should be "beyond scrutiny under the negative Commerce Clause." *Id.* (Scalia, J., dissenting).

120. *Id.* at 576.

121. *Cuno*, 386 F.3d at 746.

B. *Analysis of the Sixth Circuit Opinion*

The Sixth Circuit's decision in *Cuno* was correctly reached. The dormant Commerce Clause has been frequently assailed over the years. Sometimes, courts interpreting the doctrine have reached odd and contradictory conclusions. However, in its jurisprudence, the Supreme Court has always stated that dormant Commerce Clause questions require a case-by-case analysis.[122] Despite the fact that this case-by-case analysis is undertaken to avert any adherence to "rigid formalism," the Court's decisions have consistently reinforced certain principles as being fundamental to the dormant Commerce Clause doctrine.

The dormant Commerce Clause exists to prevent "economic protectionism."[123] To "'create [and maintain] an area of free trade among the several states,'"[124] the Supreme Court has consistently invalidated tax incentives that "'provid[e] a direct commercial advantage'"[125] to in-state business activity.[126] It is true that the Supreme Court has often said that competition among the states is "a central element of our free-trade policy."[127] But this does not permit states to undertake any and all competitive economic policies. Instead, the Court has steadfastly held on to the principle that "[s]tate laws that discriminate against interstate commerce face 'a virtually *per se* rule of invalidity.'"[128] Because the Court has invalidated a number of tax incentives, different in target and purpose, the argument that the dormant Commerce Clause

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122. *See* West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 201 (1994) ("Our Commerce Clause jurisprudence is not so rigid as to be controlled by the form by which a State erects barriers to commerce. Rather our cases have eschewed formalism for a sensitive, case-by-case analysis of purposes and effects."); *see also Westinghouse Electric*, 466 U.S. at 403; *Boston Stock Exch.*, 429 U.S. at 329. On the other hand, there is another interpretation of this case-by-case approach. *See Northwestern States Portland Cement Co.*, 358 U.S. at 457 ("That there is a 'need for clearing up the tangled underbrush of past cases' with reference to the taxing power of the States is a concomitant to the negative approach resulting from a case-by-case resolution of "'the extremely limited restrictions that the Constitution places upon the states.'" (quoting Wisconsin v. J.C. Penney Co., 311 U.S. 435, 445 (1940))).

123. *West Lynn Creamery*, 512 U.S. at 192; *New Energy Co.*, 486 U.S. at 274.

124. *Boston Stock Exch.*, 429 U.S. at 328 (quoting McLean v. J.E. Dilworth Co., 322 U.S. 327, 330 (1944)).

125. *Id.* at 329.

126. *See, e.g.*, Maryland v. Louisiana, 451 U.S. 725, 754 (1981); *Boston Stock Exch.*, 429 U.S. at 329.

127. Bacchus Imps., Ltd. v. Dias, 468 U.S. 263, 272 (1984).

128. Granholm v. Heald, 125 S. Ct. 1885, 1897 (2005) (quoting Philadelphia v. New Jersey, 437 U.S. 617, 624 (1978)).

requires narrow interpretation, one only prohibiting those incentives that "function like a tariff by placing a higher tax upon out-of-state business or products"[129] and those that rely on "both the taxpayer's in-state and out-of-state activities to determine the taxpayer's effective tax rate,"[130] misreads the Court's jurisprudence. To presume otherwise would allow form to trump substance, and permit lawmakers to craft tax policies that would pass Constitutional muster while having a discriminating economic impact.

Accordingly, the Sixth Circuit's application of Supreme Court precedent is a logical one. If a company, already located in Ohio, is looking to expand its business, it has the world available to it to decide where to invest. When making its decision, the company will examine, as DaimlerChrysler did, the Ohio ITC, which says that it can receive a tax credit *only* if it chooses to expand within the state. DaimlerChrysler's choice to stay was not "made solely on the basis of nontax criteria."[131] Thus, the ITC "forecloses tax-neutral decisions."[132] The investment tax credit uses the tax machinery of the state to coerce a business into expanding within its

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129. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 745 (6th Cir. 2004). Although the investment tax credit is not a tariff, the prohibition of these types of duties is instructive when deciding which types of tax credits are unconstitutional. A protective tariff, which the Court has described as the "paradigmatic example of a law discriminating against interstate commerce," is simply a trade mechanism that "taxes goods imported from other States, but does not tax similar products produced in State." *West Lynn Creamery,* 512 U.S. at 193. The Supreme Court stated that a tariff is "patently unconstitutional" and "violates the principle of the unitary national market by handicapping out-of-state competitors, thus artificially encouraging in-state production even when the same goods could be produced at lower cost in other States." *Id.*

130. *Cuno*, 386 F.3d at 745.

131. *Boston Stock Exch.*, 429 U.S. at 331. Professor Peter Enrich, counsel for the *Cuno* plaintiffs, argues that the dormant Commerce Clause's nondiscrimination principle should be focused on "whether a particular tax provision distorts economic decisionmaking in favor of in-state activity, not whether it treats in-state and out-of-state actors disparately." Peter D. Enrich, *Saving the States from Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 456 (1996). Professor Edward Zelinksy, however, cautions that reliance on the distortion test may effectively deem "any state tax provision discriminatory because any such provision may cause a business to invest in-state rather than out of state." Edward A. Zelinksy, Cuno v. DaimlerChrysler: *A Critique*, TAX NOTES TODAY, Oct. 11, 2004, *available at* 2004 TNT 198–45 (LEXIS).

132. *Boston Stock Exch.*, 429 U.S. at 331. *But see* Matt Kitchen, Comment, *The Ohio Investment Tax Credit: Impermissible Burden or Necessary Benefit?* Cuno v. DaimlerChrsyler, Inc., 73 U. CIN. L. REV. 1685, 1697–1700 (2005) (arguing that the Supreme Court's tax-neutrality language should be read more forgivingly than the Sixth Circuit did in *Cuno*).

borders. Therefore, the Ohio ITC discriminates against interstate commerce and is unconstitutional.[133]

V. *CUNO*'S IMPACT ON THE DORMANT COMMERCE CLAUSE AND THE USE OF ECONOMIC INCENTIVES

When the Supreme Court decides *Cuno*, it may be deciding more than just the constitutionality of the Ohio ITC. The breadth of the case's impact will depend on what direction the Court takes. Will the Court limit its decision to investment tax credits or will it issue a sweeping opinion that serves as an edict for the constitutionality of economic incentives? The Supreme Court's previous cases have shown that the Court opts for a case-by-case analysis.[134] It is not likely, therefore, that the Court's decision will reach beyond the set of tax incentives in dispute in *Cuno*. Even a narrow decision by the Court could have a wide impact on state taxation and economic policy. This section analyzes the possible impacts the decision may have on the dormant Commerce Clause and economic incentives.

A. *An Opportunity to Redefine or Reject the Dormant Commerce Clause?*

Critics of the dormant Commerce Clause have attacked it from many angles.[135] Some commentators have called for a major redefinition of the dormant Commerce Clause to remedy the "confused mishmash of elite opinion" the Supreme Court has produced in the area.[136] Others have argued that it is time for a complete rejection of the doctrine because it has "served its historic purpose, to create a single common market of the United States."[137] With two new Justices on the bench, predicting what

133. Professor Hellerstein has arrived at the same conclusion from his review of *Cuno* and earlier Supreme Court cases. *See Hearing*, *supra* note 37, at 27 (statement of Professor Walter Hellerstein).

134. *See supra* note 122 and accompanying text.

135. One commentator, in the parlance of our times, has even likened the dormant Commerce Clause to "the Voldemort of American constitutional law, a dastardly doctrine with no basis in the text of the Constitution." Jim Chen, *A Vision Softly Creeping: Congressional Acquiescence and the Dormant Commerce Clause*, 88 MINN. L. REV. 1764, 1764 (2004).

136. Granholm v. Heald, 125 S. Ct. 1885, 1923 (2005) (Thomas, J., dissenting).

137. Edward Zelinky, *Restoring Politics to the Commerce Clause: The Case for Aban-*

the Supreme Court will do in *Cuno* involves more guesswork than usual for legal prognosticators. Although the Sixth Circuit's decision in *Cuno* was one that was logically reached by application of the Supreme Court's precedent, it will be interesting to see whether the Roberts Court steadfastly applies the reasoning of prior state tax cases or whether it adds another wrinkle to the dormant Commerce Clause doctrine. If the Court's decision in *Cuno* follows the second of these scenarios, it is likely that Justice Antonin Scalia and Justice Clarence Thomas wielded great influence over their colleagues.

Justice Thomas has been the Court's sharpest critic of the dormant Commerce Clause. In his dissent in *Camps Newfound*, he echoed the typical rhetoric of the doctrine's detractors, arguing that "[t]he negative Commerce Clause has no basis in the text of the Constitution, makes little sense, and has proved virtually unworkable in application."[138] Instead of recognizing the dormant Commerce Clause, Justice Thomas might find the principle of nondiscrimination elsewhere in the Constitution. In his dissent, Justice Thomas stated he would not apply the Commerce Clause in the case, but would instead "consider restoring the original Import-Export Clause check on discriminatory state taxation to what appears to be its proper role."[139] Even with two new Justices on the bench, it is unlikely that the Supreme Court will embark on a bold doctrinal journey that would endorse Justice Thomas's position on the dormant Commerce Clause. Eventually, a textual reading of the Commerce Clause may emerge among a majority of the Justices, but even then, the Court would be hard-pressed to overturn a doctrine that is characterized as settled law.

Never coy about assailing the Supreme Court's dormant Commerce Clause jurisprudence,[140] Justice Antonin Scalia has been

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doning the Dormant Commerce Clause Prohibition on Discriminatory Taxation, 29 OHIO N.U. L. REV. 29, 29 (2002).

138. 520 U.S. at 610 (Thomas, J., dissenting); *see also* Am. Trucking Ass'ns v. Michigan Pub. Serv. Comm'n, 125 S. Ct. 2419, 2426 (2005) (Thomas, J., concurring) (arguing that the dormant Commerce Clause "'cannot serve as a basis for striking down a state statute'") (quoting Hillside Dairy Inc. v. Lyons, 539 U.S. 59, 68 (2003))).

139. *Camps Newfound*, 520 U.S. at 610. *But see* Brannon P. Denning, *Justice Thomas, The Import-Export Clause, and* Camps Newfound/Owatonna v. Harrison, 70 U. COLO. L. REV. 155, 223 (1999) ("Adopting Justice Thomas's solution would, with almost no evidence that the Framers would have approved, cut protection for interstate commerce against discriminatory and parochial state legislation to the quick.").

140. *See, e.g.*, *Am. Trucking Ass'ns*, 125 S. Ct. at 2426 (Scalia, J., concurring) ("I agree with the Court that this fee does not violate the negative Commerce Clause. Unlike the

more calculated in his criticism of the doctrine. It was Scalia, after all, who authored the Court's unanimous opinion in *New Energy*.[141] In that case, Scalia wrote that "[i]t has long been accepted that the Commerce Clause . . . directly limits the power of the States to discriminate against interstate commerce. This 'negative' aspect of the Commerce Clause prohibits economic protectionism."[142] Justice Scalia, too, engaged in a constitutional treasure hunt, seeking text that would support the theory of nondiscrimination where none can be found in the Commerce Clause. In his dissent in *Tyler Pipe Industries v. Washington State Dep't of Revenue*,[143] Justice Scalia stated that he would not expand the dormant Commerce Clause doctrine, which he described as a theory "acquired by a sort of intellectual adverse possession,"[144] but would look to the Privileges and Immunities Clause[145] to protect citizens from discrimination.[146] It is doubtful that a majority on the Supreme Court will follow this rationale, for it would be as stark a departure as sanctioning Justice Thomas's alternative. If the Roberts Court is reluctant to apply the dormant Commerce Clause or broaden it, it may adhere to Justice Scalia's language in *American Trucking Ass'ns v. Michigan Public Service Comm'n*, where Scalia suggested that he would vote against a tax incentive if it "'facially discriminates against interstate commerce and [if] it is indistinguishable from a type of law previously held unconstitutional.'"[147] Although academics are ea-

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Court, I reach that determination without adverting to various tests from our wardrobe of ever-changing negative Commerce Clause fashions."); Okla. Tax Comm'n v. Jefferson Lines, Inc., 514 U.S. 175, 201 (1995) (Scalia, J., concurring) ("I look forward to the day when *Complete Auto* will take its rightful place . . . among the other useless and discarded tools of our negative Commerce Clause jurisprudence.").

141. *See supra* notes 95–104 and accompanying text.

142. New Energy Co. of Indiana v. Limbach, 486 U.S. 269, 273 (1988).

143. 438 U.S. 232 (1987).

144. *Id.* at 265. In *Tyler Pipe*, the Supreme Court invalidated a Washington tax exemption "because it place[d] a tax burden upon manufacturers in Washington engaged in interstate commerce from which local manufacturers selling locally are exempt." *Id.* at 253.

145. U.S. CONST., art. IV, § 2, cl. 1 ("The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States.").

146. *See, e.g.*, Julian N. Eule, *Laying the Dormant Commerce Clause to Rest*, 91 YALE L.J. 425, 446–55 (1982). *But see* Brannon P. Denning, *Why the Privileges and Immunities Clause of Article IV Cannot Replace the Dormant Commerce Clause Doctrine*, 88 MINN. L. REV. 384, 414 (2003) (concluding that the "substitution of one [clause] for the other entails losing both flexibility for Congress and the states, as well as substantial protection for interstate commerce").

147. 125 S. Ct. 2419, 2426 (2005) (quoting West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 210 (1994) (Scalia, J., concurring)).

ger to see the Supreme Court address the continuing necessity of the dormant Commerce Clause and the doctrinal confusion its jurisprudence has created, the real issue is whether the Ohio ITC is indistinguishable from those laws that the Supreme Court has nullified in the past.

While the Sixth Circuit Court of Appeals—without dissent—found the Ohio ITC to be essentially indistinguishable from other unconstitutional tax changes, it is unclear whether that the Supreme Court will reach a unanimous decision as it has in many previous state tax cases.[148] This does not mean that the Court will take a significant departure from its prior opinions. Both sides of the tax incentive debate have advanced several arguments that the Justices of the Supreme Court could find credible. Considering the language of the Court's prior decisions and the apparent views of the sitting Justices, *Cuno* could be a close call. While there is disagreement over the validity of the dormant Commerce Clause and the consistency of its application, there is wide recognition that certain principles, like nondiscrimination, are well settled in the Supreme Court's jurisprudence.[149] Whether the Court invalidates or upholds the Ohio ITC, there is enough support on the bench to uphold these core principles.

B. *The Impact on Economic Incentives*

If the Supreme Court gives the State of Ohio relief on standing, the Sixth Circuit's decision in *Cuno* will be withdrawn. As a result, Ohio's ITC will stand until another legal challenge is mounted by a party that has standing against a similar tax credit. Unfortunately, this result means that the Ohio litigation, which started more than five years ago, will turn out to have been a terrible exercise of judicial economy. Ruling on standing is pref-

148. Though he testified that the Sixth Circuit applied the case law correctly in *Cuno*, *see supra* note 133, Professor Hellerstein believes that the Roberts Court will reverse the Sixth Circuit. *See* Marcia Coyle, *High Court to Hear Challenge to Company Tax Breaks*, THE NAT'L L.J., Feb. 10, 2006, *available at* http://www.law.com/jsp/ihc/PubArticleIHC.jsp?id=1139479513325.

149. *See Granholm*, 125 S. Ct. at 1908 (2005) (Stevens, J., dissenting) (arguing that if the Michigan and New York laws concerned articles of commerce other than wine, the "well settled Commerce Clause principles" would find the states' policies "patently invalid"); C & A Carbone v. Town of Clarkstown, 511 U.S. 383, 389 (1994) ("It is well settled that actions are within the domain of the Commerce Clause if they burden interstate commerce or impede its free flow.").

erable, some commentators believe, because the jurisprudence on the dormant Commerce Clause is so complex, and because it is improbable that the "case-by-case" approach the Court has taken in the past will clarify the law any further should it decide to rule on the merits in *Cuno*.[150] Nonetheless it is certain that the sentiment against economic incentives is so strong that lawsuits against tax exemptions will be filed again, forcing courts to address the scope of the doctrine of nondiscrimination as it relates to tax incentives.

1. Pursuing the Legislative Option

Because it involves the dormant Commerce Clause, the Sixth Circuit could only reach its decision in *Cuno* because Congress had not spoken on the issue. The dormant Commerce Clause doctrine prescribes that a "clearly unconstitutional, discriminatory state law will be allowed if approved by Congress because Congress has plenary power to regulate commerce among the states."[151] This premise may seem especially odd since one of the core justifications for the dormant Commerce Clause is that the American economy functions best when barriers restricting interstate commerce are removed.[152] When Congress legislates on interstate commerce regulation, other doctrines, separation of powers and federalism, prevail over the dormant Commerce Clause. In those situations, the courts, as Justice Thomas opined in *Camps Newfound*, may no longer engage in "policy-laden deci-

150. *See, e.g.*, Brannon P. Denning, *Cuno and the Court: The Case for Minimalism*, 4 GEO. J. L & PUB. POL'Y (forthcoming 2006), (manuscript at 9–11) *available at* http://ssrn.com/abstract=839345 (last visited Mar. 31, 2006). Denning reaches this conclusion by applying Professor Cass Sunstein's minimalism theory, arguing that *Cuno* is a case where the courts "'know that they may be wrong, and they know too that even if they are right, a broad, early ruling may have unfortunate systemic effects.'" *Id.* (manuscript at 9) (quoting CASS R. SUNSTEIN, ONE CASE AT A TIME: JUDICIAL MINIMALISM ON THE SUPREME COURT 26–27 (1999)).

151. ERWIN CHEMERINKSY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES 429 (2d ed. 2002). For example, the Supreme Court, in *Metro. Life Ins. Co. v. Ward*, held that it could not apply the dormant Commerce Clause to Alabama's policy of taxing out-of-state insurance companies at a higher rate than in-state companies because Congress had enacted the McCarran-Ferguson Act specifically to allow the practice. 470 U.S. 869, 880 (1985). A divided Court, however, did strike down the tax statute as violating the Equal Protection Clause, holding that the state had not advanced any legitimate state interests sought to be promoted by this discriminatory measure. *Id.* at 882–83.

152. CHEMERINKSY, *supra* note 151, at 403–04.

sionmaking" by evaluating the bounds of state taxation of interstate commerce.[153]

As such, Congress may step in to take this issue out of the Supreme Court's purview. After the Sixth Circuit's decision, Congressional leaders took action, introducing a bill "[t]o authorize the States (and subdivisions thereof), the District of Columbia, territories, and possessions of the United States to provide certain tax incentives to any person for economic development purposes."[154] Under this bill, Congress would authorize "any State to provide to any person for economic development purposes tax incentives that otherwise would be the cause or source of discrimination against interstate commerce under the Commerce Clause."[155] The bill contained seven exceptions, which Senator Voinovich, who was the governor that signed the Ohio ITC into law, claimed were created "not to authorize those tax incentives that truly discriminate against interstate commerce."[156] After the Supreme Court granted certiorari, the legislation was put on hold, but it is likely that it will be pushed through Congress if the Court upholds the lower court's decision.

Congress has the power to authorize this bill but that does not mean that it should. Senator Voinovich's bill would accelerate the so-called "race-to-the-bottom" among the states.[157] Although the bill contains several exceptions crafted to codify Supreme Court precedent in the area of state taxation, the language of the bill remains open to interpretation and challenges by foes of economic incentives. If jurists and academics find it difficult to reconcile

153. 520 U.S. 564, 620 (1977).

154. Economic Development Act of 2005, H.R. 2471, 109th Cong. (1st Sess. 2005).

155. *Id.* § 2.

156. 151 Cong. Rec. S5445 (daily ed. May 18, 2005) (statement of Sen. Voinovich).

157. *See* MAZEROV, *supra* note 16, at 2 ("While 'state sovereignty' in tax policy is generally desirable as a matter of principle, states are not sovereign in any meaningful sense when corporations are able to pit them against each other in ever-more-costly bidding wars for the latest auto or computer assembly plant."). Although the specter of a Supreme Court decision upholding *Cuno* has dissuaded some states from pursuing businesses with huge incentive packages, other states have not lost a step in the race to attract business. Last year, North Carolina offered computer manufacturer, Dell, Inc., over $280 million in state and local incentives to best its neighbors, including Virginia, to land a new plant in the state. *See* Michael Schroeder, *States Pay Steep Price to Attract Industry: Local Taxpayers, Small Businesses Bear the Burden, Say a Growing Chorus of Critics*, WALL ST. J., June 29, 2005, at A4. The package included a plan that would give Dell $225 million in income tax credits over fifteen years. *Id.* Although state officials considered the deal a big success, many residents condemned the deal that would pay 1500 people an average salary of only $28,000. *Id.*

the Court's dormant Commerce Clause jurisprudence, then it may be impossible for Congress, with complete confidence, to spare only those types of tax incentives that truly do not discriminate against interstate commerce.[158] Furthermore, future litigants may choose to attack the provisions of a counter-*Cuno* bill with arguments built upon case law related to the Equal Protection Clause, Due Process Clause, or other provisions of the Constitution.[159] Regardless of the hefty legal and economic arguments against such legislation, the political pressures might be too great for Congress to resist.[160]

2. Or Moving Toward Subsidies?

If the Supreme Court strikes down the Ohio ITC, and Congress does not act legislatively to overturn the decision, states may utilize, as Ohio already has,[161] another controversial type of economic incentive that is currently constitutional. Subsidies have been the subject of much discussion in the academic community,[162] but the

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158. As Professor Hellerstein reminded Congress, "[o]ne should not lose sight of the fact that one person's 'economic development incentive' is another person's 'discriminatory tax.'" *Hearing*, *supra* note 37, at 30 (statement of Professor Walter Hellerstein).

159. *See* JOHN E. NOWAK & RONALD D. ROTUNDA, CONSTITUTIONAL LAW 365–66 & n.6 (7th ed. 2004). These attacks may prove to be a much more difficult endeavor, however. For example, the *Cuno* plaintiffs' Equal Protection argument failed because the Sixth Circuit found that the "purpose of the Ohio statutes—to encourage industrial development and economic stimulation of the state's economically troubled areas—clearly has a reasonable nexus to the tax provisions." 386 F.3d 738, 749 (6th Cir. 2004).

The Sixth Circuit differentiated *Ward* from *Cuno*, stating that in *Ward*, Alabama imposed a discriminatory tax "in order to promote domestic industry solely based on nonresident status." *Id.* On the contrary, Ohio's statutes were constitutional because the state-made tax benefits were "equally available to domestic and foreign corporations and classif[ied] corporations on the basis of new investment in economically depressed areas." *Id.*

160. In his speech on the Senate floor, Sen. Voinovich stated: "If States choose to use tax incentives to promote economic development, then that is not a violation of the interstate commerce clause, that's simply their choice. It is called federalism, and it should not be thwarted by the courts." 151 Cong. Rec. S5445 (daily ed. May 15, 2005) (Statement of Sen. Voinovich). He added: "The challenges that manufacturers and workers face today are daunting but surmountable. The last thing we need, however, is an artificial legal hurdle that threatens to trip us up." *Id.*

161. OHIO REV. CODE. ANN. § 122.172–173 (LexisNexis 2005). In July 2005, the corporations in Ohio were able to take advantage of the new Ohio Manufacturing Machinery and Equipment Investment Grant, created to replace the ITC. The new program uses the same calculations as the ITC, but the incentive will be awarded in the form of a grant. *See* OHIO DEPARTMENT OF DEVELOPMENT, OHIO MANUFACTURING MACHINERY AND INVESTMENT GRANT PROGRAM GUIDE, *available at* http://www.odod.state.oh.us/edd/itc/M&EInvestmentGrant SummaryupdatedChuck.pdf.

162. *See, e.g.*, Dan T. Coenen, *Business Subsidies and the Dormant Commerce Clause,*

Supreme Court has "never squarely confronted the constitutionality" of incentives.[163] That is not to say that the Court has ignored the topic of subsidies altogether.

In *New Energy Company of Indiana v. Limbach*, the Court held that the Commerce Clause only prohibits discriminatory state action *"in connection with the State's regulation of interstate commerce."*[164] The Court found that "[d]irect subsidization of domestic industry does not ordinarily run afoul of that prohibition."[165] This means that the State of Ohio may give, for example, $1,000,000 in grants to businesses but not the same amount in unconstitutional tax credits for essentially the same purpose. This is an odd conclusion to reach, especially in light of the fact that the Supreme Court has been persistent in striking state tax statutes that apparently have the same economic effect as subsidies.[166] Though *New Energy* provided little insight into the constitutionality of subsidies, it left open an opportunity for the Court to fully address subsidies in a subsequent case.

The Supreme Court had its chance six years later in *West Lynn Creamery v. Healy*.[167] In *West Lynn Creamery*, the Court considered the constitutionality of a Massachusetts pricing order that placed "an assessment on all fluid milk sold by [milk] dealers to [state] retailers."[168] The pricing order required milk dealers[169] to pay a monthly fee into the Massachusetts Dairy Equalization Fund.[170] From the Fund, each state producer received a subsidy

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107 YALE L.J. 965 (1998); Christopher R. Drahozal, *On Tariffs v. Subsidies in Interstate Trade: A Legal and Economic Analysis*, 74 WASH. U. L.Q. 1127 (1996); Note, *Functional Analysis, Subsidies, and the Dormant Commerce Clause*, 110 HARV. L. REV. 1537 (1997).

163. *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 199 n.15 (1994).

164. 486 U.S. 269, 278 (1988).

165. *Id.*

166. *Cf. Westinghouse Elec.*, 466 U.S. at 406–07 ("When a tax, on its face, is designed to have discriminatory economic effects, the Court 'need not know how unequal the Tax is before concluding that it unconstitutionally discriminates.'" (quoting Maryland v. Louisiana, 451 U.S. 724, 760 (1951))); *Boston Stock Exch.*, 429 U.S. at 334 n.13 ("[T]he Clause protects out-of-state businesses from *any* discriminatory burden on their interstate commercial activities.") (emphasis added).

167. 512 U.S. 186 (1994).

168. *Id.* at 188. The pricing order was set in response to a commission finding that a majority of the few dairy producers left in the state would go out of business within the year if milk prices did not increase. *Id.* at 189.

169. Defined as "any person who is engaged within the Commonwealth in the business of receiving, purchasing, pasteuruizing, bottling, distributing, or otherwise handling milk, purchases or receives milk for sale as the consignee or agent of a producer." *Id.* at 190 n.4.

170. *Id.* at 188–91.

equal to its "proportionate contribution to the State's total production of raw milk."[171] Two milk dealers licensed to do business in Massachusetts brought suit against the state, claiming that the pricing order violated the Commerce Clause.[172] The Court stated that the payments made to the Fund were "effectively a tax which makes milk produced out of State more expensive."[173] As a result, the Court held that the pricing order was unconstitutional because its "purpose and its undisputed effect are to enable higher cost Massachusetts dairy farmers to compete with lower cost dairy farmers in other States."[174]

Massachusetts argued that its subsidy program was constitutional because the payments were a nondiscriminatory tax and that it could subsidize its farmers through the use of a permissible tax.[175] The Court rejected the idea that the subsidy program was purely a "combination of two independently lawful regulations."[176] On the contrary, the Court held that "[b]y conjoining a tax and a subsidy, Massachusetts has created a program more dangerous to interstate commerce than either part alone."[177] The rationale behind this decision is intriguing. The majority held that the tax and subsidy arrangement meant that the Commonwealth's political processes could "no longer be relied upon to prevent legislative abuse, because one of the in-state interests which would otherwise lobby against the tax has been mollified by the subsidy."[178] In other words, the lack of a "political check" on the subsidy program doomed it.[179] Justice Rehnquist, in dissent, disagreed, stating that "[a]nalysis of interest group participation in

171. *Id.* at 191. There was an upper limit to the subsidy, however. Farmers that produced more than 200,000 pounds of milk were deemed to have produced only 200,000 pounds. *Id.* at 191 n.8.

172. 512 U.S. at 191.

173. *Id.* at 194. The fact that Massachusetts milk producers also made the payments did not save the program because the effect on state producers was "entirely (indeed more than) offset by the subsidy provided exclusively to Massachusetts dairy farmers." *Id.*

174. *Id.*

175. *Id.* at 198–99.

176. *Id.* at 198.

177. *Id.* at 199–200.

178. *Id.* at 200. The Court reasoned that the dairy farmers, milk dealers, and consumers affected by the pricing order would have typically lobbied against the policy. The dairy farmers, however, would advocate for the tax because they benefited from it. *Id.* at 200–01.

179. *See id.* at 200 n.17; *see also* NOWAK & ROTUNDA, *supra* note 159, at 321–22 ("The phrase 'inner political check' refers to the fact that all local persons affected by local legislation have the opportunity to participate in the democratic process that produces such legislation.").

the political process may serve many useful purposes, but serving as a basis for interpreting the dormant Commerce Clause is not one of them."[180] Justifying different treatment of tax incentives and subsidies based on political process grounds may seem extraordinary considering the indistinguishable economic impact,[181] but several commentators have supported this idea.[182]

This "political check" theory commands that tax incentives are "typically independent" of state budget processes, are "less politically visible" than subsidies, have indeterminate costs, and "do not have to compete with other demands on state resources in the appropriation process."[183] For these reasons, Professors Hellerstein and Coenen argue that states should move toward subsidies

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180. *West Lynn Creamery*, 512 U.S. at 215 (Rehnquist, C.J., dissenting). Justice Scalia and Justice Thomas concurred in the judgment, but disagreed on how the Court reached its decision. *Id.* at 207 (Scalia, J., concurring). Although the Court did not consider the constitutionality of subsidies, Justice Scalia argued that "a state subsidy would *clearly* be invalid under any formulation of the Court's guiding principle." *Id.* at 208 (Scalia, J., concurring). Justice Scalia proposed that there were four measures that Massachusetts could have taken to produce their intended effect:

> (1) a discriminatory tax upon the industry, imposing a higher liability on out-of-state members than on their in-state competitors; (2) a tax upon the industry that is nondiscriminatory in its assessment, but that has an "exemption" or "credit" for in-state members; (3) a nondiscriminatory tax upon the industry, the revenues from which are placed into a segregated fund, which fund is disbursed as "rebates" or "subsidies" to in-state members of the industry (the situation at issue in this case); and (4) with or without nondiscriminatory taxation of the industry, a subsidy for the in-state members of the industry, funded from the State's general revenues.

Id. at 210 (Scalia, J., concurring). According to Justice Scalia, the Supreme Court's jurisprudence clearly supports the notion that the first two measures are unconstitutional. *Id.* at 210–11 (Scalia, J., concurring). Justice Scalia's rationale for concurring in the decision was that the pricing order, in effect, was the third measure. *See id.* at 211 (Scalia, J., concurring). The only difference between the second and third measure was one of form, and could therefore not be held constitutional. *Id.* at 210–11 (Scalia, J., concurring).

In addition, Justice Scalia believed that the fourth measure was "so far removed from what we have hitherto held to be unconstitutional, that prohibiting it must be regarded as an extension of our negative-Commerce-Clause jurisprudence and therefore, to me, unacceptable." *Id.* at 211 (Scalia, J., concurring). Finally and perhaps most importantly, Justice Scalia noted that the Supreme Court had already approved subsidies even though the Court had declared that it had not yet taken on the issue directly. *Id.* (Scalia, J., concurring) (citing Hughes v. Alexandria Scrap Corp., 426 U.S. 794, 809–10 (1976)).

181. *See* Hellerstein & Coenen, *supra* note 14, at 868 ("[T]he economic consequences of tax breaks and subsidies are often indistinguishable."). *But see* Zelinksy, *supra* note 137, at 70–76.

182. *See, e.g.*, Hellerstein & Coenen, *supra* note 14, at 869 (arguing that the "consideration of a subsidy forces the mind of the public body to consider most pointedly the cost and consequences of moving forward"). *But see* Zelinsky, *supra* note 137, at 70–76.

183. Evelyn Brody, *Charities in Tax Reform: Threats to Subsidies Overt and Covert*, 66 TENN. L. REV. 687, 748–49 n.254 (1999) (quoting Enrich, *supra* note 131, at 442–43).

and away from tax incentives because the former focuses "state decisionmakers—and the voters to whom they are accountable—on the costs and inequities that business development incentives can engender."[184] Even though transparency of and accountability in the political process are significant concerns,[185] economic incentives are so widespread and the fear of job loss is so great that it is questionable whether the political check operates with any force today.

For decades, the courts, following the Supreme Court's case law, have struck down tax incentives that have burdened interstate commerce. These tax incentives were discriminatory and placed barriers to a national marketplace. Meanwhile, the Court passed on deciding the constitutionality of subsidies. As a result, states have used enormous subsidies to attract business.[186] For scholars and legislators, this reality is controversial and confusing. After all, the Supreme Court has taken the position that the Constitution views two incentives completely differently even though their effects might be the same. This peculiar notion needs to be revisited. If the Roberts Court continues to take the case-by-case approach in dealing with the dormant Commerce Clause, the Justices will once again note the subsidy conundrum, but pass on trying to solve it.[187]

VI. CONCLUSION

Cuno is closely watched because the position the Supreme Court takes will greatly affect the way states conduct business. The case has highlighted the significant disagreement over the role of tax incentives in attracting businesses to a region. At the heart of this controversy is the dispute over the judiciary's role in second-guessing the public policy decisions of state legislatures. Even though the legislatures should decide which tax incentive is best for their states, the Supreme Court cannot shy away from evaluating and invalidating tax policies that discriminate against interstate commerce. If it does withdraw its review of such eco-

184. Hellerstein & Coenen, *supra* note 14, at 870.

185. *See* Coenen, *supra* note 162, at 998–1002.

186. *See* Good Jobs First, Largest Subsidy Deals, http://www.goodjobsfirst.org/corporate_ subsidy/reference_ material.cfm (last visited Mar. 31, 2006).

187. In fact, the Justices did not let the parties elude the subsidy issue during oral argument. *See* Transcript of Oral Argument, *supra* note 23, at 26–27, 44–46.

nomic policies, the Court risks allowing burdens to be placed on the national marketplace, a condition hostile to the dormant Commerce Clause.

At the same time, the Supreme Court can decide *Cuno* without passing judgment on the efficacy of tax incentives. In *Cuno*, the Supreme Court is considering the constitutionality of the Ohio investment tax credit. The *Cuno* plaintiffs have not asked the Court to extend its powers of review beyond those previously used in prior state tax cases. In those prior cases, however, the Supreme Court left legislatures without clear guidance in crafting constitutional tax incentives. Even worse, the Court's silence on the issue of subsidies have placed its reasoning in many of those cases on shaky ground, as the economic effects of subsidies and unconstitutional tax incentives appear to be indistinguishable. In this light, *Cuno* presents an opportunity for the Court to depart from its usually narrow focused, case-by-case approach to the dormant Commerce Clause in order to clarify the inconsistencies in its jurisprudence.

Alternatively, Congress may legislate around *Cuno* and overrule the courts. Either way, it could be extremely difficult for the Supreme Court or Congress to reconcile the apparent ambiguities of this cloudy area of law. However, both Congress and the Court must recognize that one rule shines through the haze of Supreme Court's dormant Commerce Clause opinions—states may not use their taxing power to coerce businesses into staying, expanding, or locating within their boundaries.

S. Mohsin Reza

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