Location Incentives and the Negative Commerce Clause: A Farewell to Arms?

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LOCATION INCENTIVES AND THE NEGATIVE COMMERCE CLAUSE:
A FAREWELL TO ARMS?

I. INTRODUCTION

Economists describe incentives as the "key to solving just about any riddle."¹ In the rising competition for mobile capital, state and local governments clearly embrace this description.² From movie production³ to automobile manufacturing,⁴ sub-national government uses economic incentives as the standard-issue means to encourage local growth and development.⁵

These location incentives, which critics derisively term "corporate welfare" and "entitlements,"⁶ are as controversial as they are ubiquitous.⁷ Detractors of location incentives argue that sub-national competition for mobile capital has devolved into a "'prisoners' dilemma,' in which individually rational behavior is nonetheless collectively irrational."⁸ The ensuing race to the bottom has been characterized as the "second Civil War."⁹ Even so, state and local legislatures seem neither willing nor able to disarm unilaterally.¹⁰

It remains undisputed that "State[s] may . . . compete with other States for

⁵. See LeRoy, supra note 2, at 16.
¹⁰. See THOMAS, supra note 7, at 9 ("The cost of not offering location subsidies when other jurisdictions are doing so is lost investment.").
a share of interstate commerce."\textsuperscript{11} Competition, however, is not without limits. In recent decades, the United States Supreme Court repeatedly invalidated state and local tax incentives for violating the "dormant" or "negative" aspect of the Commerce Clause.\textsuperscript{12} Eschewing constitutional delineation, the Supreme Court addressed such incentives on a case-by-case basis.\textsuperscript{13} The resulting negative Commerce Clause jurisprudence has been called "tortuous."\textsuperscript{14} Indeed, the Court "has left 'much room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation.'"\textsuperscript{15}

This Comment addresses the current state of location incentives under the negative Commerce Clause. Part II provides a brief historical background of the use of location incentives in the United States. Part III outlines the Supreme Court's negative Commerce Clause jurisprudence. Part IV analyzes recent case law addressing sub-national taxation under the negative Commerce Clause. Here, this Comment argues that the current state of the law is inconsistent with modern limits imposed by "positive" Commerce Clause jurisprudence.\textsuperscript{16} Last, Part V offers a brief conclusion.

II. THE HISTORY OF LOCATION INCENTIVES IN THE UNITED STATES

In the bestseller \textit{Freakonomics}, rouge economist Steven Levitt argues that "humans respond to incentives."\textsuperscript{17} The history of location incentives in the United States bears witness to this statement. Since the colonial era, economic incentives have been the recognized means to attract and retain local commerce and industry.\textsuperscript{18}

New Jersey offered the earliest known state-level location incentive to Alexander Hamilton in 1791.\textsuperscript{19} Accepting the state's inducement, Hamilton agreed to locate a manufacturing facility in Paterson, New Jersey.\textsuperscript{20} Even

\begin{itemize}
  \item \textsuperscript{12} See id. at 329 (discussing the history of negative Commerce Clause jurisprudence).
  \item \textsuperscript{13} See id.
  \item \textsuperscript{14} See Enrich, \textit{supra} note 9, at 425.
  \item \textsuperscript{15} \textit{Boston Stock Exch.}, 429 U.S. at 329 (quoting \textit{Nw. States Portland Cement Co. v. Minnesota}, 358 U.S. 450, 457 (1959)).
  \item \textsuperscript{17} See \textit{LEVITT & DUBNER}, \textit{supra} note 1, at 7.
  \item \textsuperscript{19} See id. The incentive exempted the Hamilton's facility from "all taxes[,] charges[,] and impositions whatsoever." \textit{Id}.
  \item \textsuperscript{20} \textit{Id}.
\end{itemize}
though the Paterson facility generated roughly 20,000 new jobs, critics derided the location incentive as "'injurious to . . . other states'" and "'[a] most unjust and arbitrary law[].'"\footnote{21}

Two centuries later, critics still contend that location incentives are injurious, unjust, and arbitrary.\footnote{22} Nevertheless, the use of location incentives has proliferated.\footnote{23} The modern location incentive owes its pedigree to the southern states of the Great Depression, which offered property tax abatements to attract new industry.\footnote{24} These abatements served as a catalyst, energizing the southern states’ stagnant economies and drawing imitation from other states.\footnote{25}

Nowadays nearly every state seems to offer some form of location incentive.\footnote{26} State and local governments award an estimated $48.8 billion in incentives annually.\footnote{27} Meanwhile, competition for mobile capital between sub-national government, as well as international localities, appears to be increasing.\footnote{28} Amidst this escalating competition, the prevalence of state and local incentives packages will likely continue to rise.\footnote{29}

### III. NEGATIVE COMMERCE CLAUSE JURISPRUDENCE

The negative Commerce Clause limits the permissible scope in which state and local government may utilize their taxation powers.\footnote{30} It is a bedrock premise of constitutional law that "taxes . . . [which] formally discriminate against interstate or foreign commerce are forbidden."\footnote{31} In \textit{Complete Auto Transit, Inc. v. Brady},\footnote{32} the Supreme Court jettisoned formalistic reasoning\footnote{33}
that "attach[ed] constitutional significance to a semantic difference,"\textsuperscript{34} instead adopting a four-factor approach to state and local taxation.\textsuperscript{35}

The constitutional analysis announced by the Supreme Court in \textit{Complete Auto Transit} is highlighted by the third factor—nondiscrimination.\textsuperscript{36} The Supreme Court visited this factor in a tetralogy of decisions over the last two decades, each time invalidating state taxation schemes containing geographical limitations.\textsuperscript{37}

\textit{A. Boston Stock Exchange v. State Tax Commission}

The first in the series of cases, \textit{Boston Stock Exchange v. State Tax Commission},\textsuperscript{38} established the rubric for analyzing the \textit{Complete Auto Transit} nondiscrimination factor. In \textit{Boston Stock Exchange}, the Supreme Court reversed the decision of the New York State Court of Appeals, which upheld the constitutionality of an amendment to New York's securities taxation scheme.\textsuperscript{39} Six regional stock exchanges challenged the New York securities tax provision—a fifty percent rate reduction on nonresident in-state sales and a cap on total tax liability for single transactions occurring in New York—alleging that the statute violated the Commerce Clause.\textsuperscript{40} The court of appeals dismissed the complaint, reasoning that the amended New York securities tax furthered the state's legitimate interest in stimulating the growth

\begin{verbatim}

33. Before \textit{Complete Auto Transit, Inc.}, the Supreme Court routinely distinguished "direct" from "indirect" taxation, invalidating the former while upholding the latter. See, e.g., \textit{Freeman v. Hewit}, 329 U.S. 249, 256 (1946).
34. 430 U.S. at 285.
35. The four factors—substantial nexus to the taxing state, fairly apportioned, nondiscriminatory, and fairly related to state services—ignore linguistics, focusing instead on the practical effect of state taxation. \textit{Complete Auto Transit, Inc.}, 430 U.S. at 279.
36. See \textit{Enrich}, supra note 9, at 426 ("[T]he antidiscrimination prong is of primary significance.").
37. See infra Part III.A-D.
39. See id. at 337.
40. \textit{id.} at 324.
41. \textit{id.} at 320. New York's amended securities tax required at least one "taxable event" to occur in-state. New York broadly defined a taxable event to include "all sales... and all deliveries or transfers of shares or certificates of stock." \textit{id.} at 321. Prior to the amendment, New York tax liability arose on the occurrence of a single in-state taxable event notwithstanding the location of the rest of the transaction. \textit{id.} at 330. Following the amendment, a perspective nonresident taxpayer had two options: "If he elected to sell on an out-of-state exchange, ... [a] higher [tax] rate[,] ... applied without limitation on total tax liability; [but] if he sold... on [the] New York exchange, ... [a] one-half rate ... applied." \textit{id.} at 330-31. Resident taxpayers subject to the full securities transfer tax could limit total tax liability by transacting wholly in the State of New York. \textit{id.} at 330 n.11.

\end{verbatim}
and development on the New York Stock Exchange. The Supreme Court reversed the judgment.

The Court began its analysis by acknowledging "the national interest in free and open trade" protected by the Commerce Clause and the legitimate interest of states in raising tax revenue. Carefully balancing these countervailing policy considerations, the Court noted that a basic principle emerged. Specifically, "[n]o State, consistent with the Commerce Clause, may 'impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business.'"

Therefore, the Court reasoned, the basic question before it was whether the taxation scheme "discriminate[d] between two types of interstate transactions in order to favor local commercial interests over out-of-state businesses." Unlike the "compensatory" taxes the Court upheld in its prior decisions, New York's amended securities tax, in practice, increased the amount of in-state transactions at the expense of business conducted in other states. The principle of free and open trade, the Court explained, barred New York from leveraging its taxation power over in-state transactions in a manner that diverted interstate commerce and diminished free market competition. Hence the Court invalidated the amended New York securities tax.

42. Id. at 328.
43. Id. at 324.
44. Boston Stock Exch., 429 U.S. at 329.
45. Id. at 328-29.
46. Id.
47. Id. (quoting N.W. States Portland Cement Co. v. Minnesota, 358 U.S. 450, 458 (1959) (alteration in original)).
48. Id. at 335.
49. See, e.g., Henneford v. Silas Mason Co., 300 U.S. 577, 583-84 (1937) ("Equality is the theme that runs through" a valid compensatory tax scheme. "There shall be a tax . . . , but subject to an offset if another . . . tax has been paid for the same thing."). New York's securities taxation, however, resulted in inequality: The amended tax "foreclose[d] tax-neutral decisions" by raising out-of-state tax liability to the benefit of in-state business. See Boston Stock Exch., 429 U.S. at 330-32.
51. See id. at 336.
52. In conclusion, the Court explained,

Our decision today does not prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry. . . . We hold only that in the process of competition no State may discriminatorily tax the products manufactured or the business operations performed in any other State.

Id. at 336-37.
B. Westinghouse Electric Corp. v. Tully

Nearly a decade later, the Supreme Court again invalidated a New York tax incentive in Westinghouse Electric Corp. v. Tully. Westinghouse filed a lawsuit challenging a New York tax provision that enabled certain corporations to offset franchise tax liability with a credit limited to the gross receipts of exports shipped from New York. According to Westinghouse, the geographical limitation imposed by the New York export credit ran afoul of the negative Commerce Clause’s nondiscrimination principle; the Supreme Court agreed.

Relying heavily on precedent, the Supreme Court rejected the argument that the burden the tax imposed on “interstate commerce [was] not of constitutional significance.” Rather, the franchise tax credit was directly proportional to the exports shipped from New York; put another way, the tax provided a “positive incentive for increased business activity” in-state, while simultaneously penalizing increases in business activity in other states. Therefore, the Court reasoned, the tax scheme at issue was indistinguishable from the taxation schemes it previously invalidated in Boston Stock Exchange and Maryland v. Louisiana—in each case the challenged tax scheme “foreclose[d] tax-neutral behavior.”

The Supreme Court also rejected the argument that New York’s franchise tax credit was somehow an indirect subsidy:

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54. Id. at 390. The challenged New York tax neutralized the perceived effect of congressional changes to the Internal Revenue Service Code. See id. Under the new law, Congress exempted from federal income taxation Domestic International Sales Corporations (DISCs), which would have cost New York State an estimated $20–30 million in lost tax revenue because federal income tax liability formed the basis of New York’s franchise tax allocation. See id. at 392. Alternatively, if New York amended its franchise tax allocation to assess taxation on DISC income directly, the tax might have discouraged in-state DISC formation and the manufacture of export goods within New York. See id. at 392-93. As a result, New York enacted legislation pertaining specifically to DISC taxation; the enacted provisions incorporated “a partially off-setting tax credit” that was “limited to gross receipts from export products ‘shipped from a regular place of business . . . within [New York].’” Id. at 393. Westinghouse took issue with this geographical limitation. See id. at 395-96.
55. Id. at 396.
56. Id. at 405.
57. Id. at 401.
58. Westinghouse Elec. Corp., 466 U.S. at 404. In Maryland v. Louisiana, 451 U.S. 725, 725 (1981), the Supreme Court struck down Louisiana’s “first-use” tax, which the state imposed on natural gas imports not subject to taxation in any other state. According to the Court, the first-use tax “unquestionably discriminate[d] against interstate commerce in favor of local interests. . . . No further hearings [we]re necessary . . . .” Id. at 754.
59. Id. at 429 (quoting Boston Stock Exch. v. State Tax Comm’n, 429 U.S. 318, 331 (1977)).
The Tax Commission seeks to classify the tax credit at issue here as an indirect subsidy to export commerce, similar to provision and maintenance of ports, airports, waterways, and highways; to provision of police and fire protection; and to enactment of job-incentive credits and investment-tax credits. We reiterate that it is not the provision of the credit that offends the Commerce Clause, but the fact that it is allowed on an impermissible basis, i.e., the percentage of a specific segment of the corporation's business that is conducted in New York.  

Accordingly, the Court concluded that "[t]he manner in which New York allow[ed] corporations a tax credit on the accumulated income . . . violat[ed] the Commerce Clause".  

C. Bacchus Imports, Ltd. v. Dias

In Bacchus Imports, Ltd. v. Dias, the Supreme Court reversed the judgment of the Hawaii Supreme Court, affirming the dismissal of a lawsuit involving Hawaii's liquor tax exemption for beverages manufactured from indigenous plants. The dispute arose when in-state liquor wholesalers sued, alleging that the tax exemption impermissibly burdened interstate commerce.

As a threshold matter, the Supreme Court observed that the "tax exemption . . . at issue seem[ed] clearly to discriminate on its face." Not surprisingly the Court found Hawaii's argument that the tax-exempt liquor did not pose a "competitive threat" unpersuasive and misplaced. The contention that there was no competition between indigenous and foreign liquor was belied by legislative intent indicating Hawaii's desire to stimulate local industry by encouraging consumption of indigenous liquor.

60. Westinghouse Elec. Corp., 466 U.S. at 406 n.12 (internal citations omitted).
61. Id. at 407. The Court reinforced the case-by-case approach articulated in Boston Stock Exchange: "We hold only that in the process of competition no State may discriminatorily tax the products manufactured or the business operations performed in any other State." Id. at 406-07 n.12.
63. Id. at 266-67. Under Hawaii's liquor taxation, the state assessed a twenty-percent excise tax on liquor sales; however, sales of okolehao brandy (made from the indigenous ti root) and pineapple wine were tax-exempt. Id. at 263.
64. Id. at 265.
65. Id. at 268.
66. Id. at 269.
67. Id.
the Court explained, whether competition existed or not was inconsequential as to the question of discrimination.68 Hawai'i's justification for its liquor taxation scheme—as a means to subsidize a struggling, largely nonexistent industry—also proved irrelevant.69 Unmoved by this line of argument, the Supreme Court reaffirmed that the Constitution proscribes state taxation that "build[s] . . . [in-state] commerce by means of unequal and oppressive burdens upon the industry and business of other States."70

D. New Energy Co. of Indiana v. Limbach

In New Energy Co. of Indiana v. Limbach,71 the last in the series of major decisions discussing the nondiscrimination factor, the Supreme Court struck down an Ohio tax credit with a geographical limitation.72 New Energy, an Indiana corporation, filed suit seeking declaratory and injunctive relief after Indiana repealed its ethanol credit, which prevented the corporation's clients from claiming the Ohio ethanol credit.73

Writing for the unanimous majority, Justice Scalia declared that the Ohio tax credit "violat[ed] the cardinal requirement of nondiscrimination"—expressly depriving out-of-state industry (ethanol producers) of the same favorable taxation as in-state industry.74 Nonetheless, Ohio argued that the availability of the tax credit to some out-of-state ethanol producers cured the constitutional infirmity of the challenged taxation scheme.75 The Court rejected the argument, explaining that the states cannot use facially discriminatory taxation "as a weapon to force sister States to enter into even a desirable reciprocity agreement."76 This type of facial discrimination, according to the Court, warranted the "strictest scrutiny," a standard under which the unanimous majority had little difficulty invalidating Ohio's taxation scheme.77

68. Id.
69. Id. at 268-69.
70. Id. at 272 (quoting Guy v. Baltimore, 100 U.S. 434, 443 (1880)).
72. Id. Prior to 1984 Ohio offered the ethanol credit to dealers notwithstanding the ethanol's source; however, in that year Ohio enacted the challenged provision, restricting the tax credit to ethanol produced in-state or in a state with a similar ethanol credit. Id.
73. Id.
74. Id. at 274.
75. Id.
76. Id. (quoting Grant Atl. & Pac. Tea Co. v. Cottrell, 424 U.S. 366, 379 (1976)).
77. New Energy Co., 486 U.S. at 274-75.
In dicta, Justice Scalia addressed subsidization and the so-called "reasonable nondiscriminatory alternative[]" defense. Unlike Ohio, the State of Indiana directly subsidized in-state ethanol production for which New Energy was eligible. That the practical effect of direct subsidization may mirror the effect of discriminatory taxation is constitutionally irrelevant: "Direct subsidization of domestic industry does not ordinarily run afoul of . . . [the Commerce Clause]." However, the Court noted, "discriminatory taxation of out-of-state manufacturers does."

The Supreme Court acknowledged that its holding did not foreclose the argument that an apparently discriminatory tax advanced "a legitimate local purpose that . . . [could not] be adequately served by reasonable nondiscriminatory alternatives." The Court left little doubt that the standards for establishing such a justification are high. Accordingly, the Court dismissed Ohio's proffered justifications—health and commerce—as "implausible speculation."

IV. LOCATION INCENTIVES UNDER THE NEGATIVE COMMERCE CLAUSE

Following New Energy Co., the precise mete and bound of the nondiscrimination factor remains illusive; the distinction "between the constitutional carrot and the unconstitutional stick" remains ill-defined. Ostensibly limiting itself to the peculiar facts and circumstances of each case, the Supreme Court's often expansive language leaves doubt as to whether the nondiscrimination factor has any limit.

The Supreme Court, nonetheless, repeatedly has reinforced the notion that states are free to "structur[e] their tax systems to encourage the growth and development of interstate commerce and industry." Juxtaposed against this

78. Id. at 278.
79. Id.
80. Id.
81. Id.
82. Id.
83. New Energy Co., 486 U.S. at 278.
84. Id. at 280. ("In sum, appellees' health and commerce justifications . . . do[] not suffice to validate this plain discrimination . . . .").
87. See Hellerstein & Coenen, supra note 85, at 805.
88. See Boston Stock Exch., 429 U.S. at 336. In a similar vein, the Court has entertained health and safety justifications to remedy a statute that it found to discriminate facially against interstate commerce. See supra note 84 and accompanying text.
principle is the Commerce Clause precept of free and open trade among the "several States." The debate regarding the constitutionality of state and local location incentives lies at the center of these divergent policy considerations.

Until recently, the notion that location incentives might violate the negative Commerce Clause was mere theory. The Sixth Circuit's opinion in Cuno v. DaimlerChrysler, however, asserts otherwise. That case posits an "anti-coercion" standard for analyzing nondiscrimination under Complete Auto Transit test. The basis for this standard rests in academic literature.

A. The Anti-Coercion Standard

In their seminal article, Professors Hellerstein and Coenen offer a "more restrained approach" to negative Commerce Clause jurisprudence centered on the concept of anti-coercion. Under the anti-coercion standard, there is a constitutional proscription against state and local governments using the taxation power to coerce business decisions. State and local governments are forbidden from effectively saying,

You [target business or industry] are already subject to our taxing power because you engage in taxable activity in this state. If you would like to reduce your tax burdens, you may do so by directing additional business activity into this state. Should you decline our invitation, we will continue to exert our taxing power over you as before, and your tax bill might even go up.

Hence state and local tax exemptions or reductions (such as the one at issue in Cuno) would be constitutionally infirm. In other words, the anti-coercion

89. U.S. CONST. art. I, § 8, cl. 3; see also Boston Stock Exch., 429 U.S. at 329.
90. See, e.g., Enrich, supra note 9 (arguing that location incentives violate the negative Commerce Clause by distorting business decisions in the favor of in-state economic interests).
91. 386 F.3d 738 (6th Cir. 2004) (invalidating an Ohio investment tax credit for discriminating against interstate commerce), cert. granted, 126 S. Ct. 356 (2005).
92. See id. at 740.
93. See Hellerstein & Coenen, supra note 85, at 804, 809 (arguing a "coercion-centered analysis" would help harmonize the states' interest in fostering economic growth through the taxation power with the Commerce Clause's anti-protectionist underpinnings).
94. See generally id. at 804-13.
95. Id. at 808.
96. To further illustrate, consider two state tax exemptions: $S_1$ that applies a credit to future tax liability on new investment; and $S_2$ that applies a credit against existing tax liability, but the credit is
standard prohibits a state from leveraging the "constitutional carrot"—the permissible legislative methods aimed at fostering economic and growth development—against its authoritative power.  

B. Cuno v. DaimlerChrysler

In Cuno, the Sixth Circuit Court of Appeals legitimized the anti-coercion standard when it struck down Ohio's franchise tax credit, despite affirming the constitutionality of the states' property tax abatement. The case arose when DaimlerChrysler agreed to build a billion-dollar assembly plant near its existing facility in Toledo, Ohio, thereby becoming eligible to receive a franchise tax credit and property tax abatement. The plaintiffs—residents of Ohio and Michigan—brought the underlying lawsuit arguing that these incentives violated the negative Commerce Clause. The court of appeals partially agreed.

Relying extensively on Boston Stock Exchange and its progeny, the court began its analysis by recognizing Ohio's legitimate use of the "tax system to encourage new intrastate economic activity." Nonetheless, the court explained, the negative Commerce Clause prohibits state and local taxation that (a) facially discriminates against interstate commerce or (b) discriminates against interstate commerce in purpose and effect by "providing a direct

also contingent on new investment. Under the anti-coercion standard, $S_1$ is constitutionally permissible, while $S_2$ violates negative Commerce Clause prohibitions. Unlike the former that embodies a policy decision to exempt a "virgin' tax base," $S_2$ has the effect of "coercing" new business by offering to lower in-state tax liability. See id. at 809.

97. See id. at 792, 825–29. But see Edward A. Zelinsky, Restoring Politics to the Commerce Clause: The Case For Abandoning the Dormant Commerce Clause Prohibition on Discriminatory Taxation, 29 OHIO N.U. L. REV. 29 (2002) (arguing that notwithstanding tax-related coercive, business decisions with respect to location are volitional so long as the business knows the terms attached to the state or local incentive packages up-front).

98. See Cuno, 386 F.3d at 747. According to the court, the challenged tax provision, a franchise tax credit, effectively coerced business to reinvest in-state through the concomitant denial of preferential tax treatment for out-of-state commercial activity. In effect, the "constitutional carrot" (the legitimate use of Ohio's taxation power) was impermissibly leveraged against the unconstitutional use of the state's authoritative power (linking tax credit eligibility to increased in-state commercial activity). See id. at 746.

99. See id. at 748

100. Id. at 741–42. Notably, DaimlerChrysler was eligible for a 13.5 percent credit against existing franchise tax liability, in addition to property tax abatements on machinery and equipment "first used in business at the [in-state] project site." Id. at 742.

101. Id. at 741.

102. Id. at 746.

103. Id. at 742.
commercial advantage to local business.”104 The franchise tax credit ran
afoul of the latter prohibition—its subtle operation “encourage[d] further
investment in-state at the expense of [out-of-state] development,”105 thus,
hindering the “free trade among the states.”106

The court was not persuaded by the defendants’ efforts to cure the tax
 provision of its constitutional infirmities.107 First, the court rejected the
defendants’ narrow construction of negative Commerce Clause precedent,
which sought to distinguish “laws that benefit in-state activity . . . [from] laws
that burden out-of-state activity.”108 According to the court, such a “tenuous”
distinction ignored the well-established principle that “a tax statute’s
‘constitutioality does not depend upon whether one focuses upon the
benefited or burdened party.”109

Equally inapposite was the defendants’ argument that the franchise tax
credit should be treated as a subsidy.110 Although a direct subsidy would
produce the same economic effect as the franchise tax credit, the court
emphasized that the former is constitutionally distinct because it does not
involve “state regulation of interstate commerce through the power to tax.”111
Hence, the court explained, the franchise tax credit failed due to its coercive
effect on business location decisions.112

The property tax abatement, the court reasoned, produced a contrary
purpose and effect.113 Unlike the coercive attributes of the franchise tax
credit, the property tax abatement did not impermissibly relate “favorable tax
treatment . . . to the use or location of the property itself.”114 Instead, a
prospective corporate taxpayer’s “failure to locate new investments within
Ohio simply mean[t] that the taxpayer [wa]s not subject to the state’s property
tax at all.”115 At any rate, since the property tax abatement failed in effect to

104. Cuno, 386 F.3d at 743 (quoting Bacchus Imps., Ltd., 486 U.S. at 268).
105. Id. at 746.
106. See id.
107. See id. at 745-46.
108. Id. at 745.
109. Id. at 743, 745-46.
110. Id. at 746.
111. Id.
112. See id. & n.1.
113. See id. at 746-48.
114. Id. at 746.
115. Id. at 747. Of course, the same argument could be made in favor of the franchise tax
credit. Because the franchise tax credit is contingent upon new in-state investment, total franchise
tax liability likely will fluctuate inversely with out-of-state investment: out-of-state investment
effectively would limit a prospective business taxpayer’s value and activity in-state for the purpose
of in-state franchise tax allocation. If the business is cognizant of the trade-offs, there is no
coevolution. See Zelinsky, supra note 97. The choice, therefore, becomes whether the business prefers
coerce prospective taxpayers into increasing in-state business activity (or forestalling out-of-state activity), the provision did not offend the negative Commerce Clause.

C. Anti-Coercion and the Scope of "Nondiscrimination"

The Sixth Circuit's adoption of the anti-coercion standard extends the scope of the nondiscrimination factor, reaching past the narrow question of the state of Ohio's franchise tax credit. In fact, under the standard announced in Cuno, most state and local taxation measures appear constitutionally suspect. The anti-coercion standard, furthermore, appears unworkable as evidenced by the Sixth Circuit's apparent failure in Cuno to reconcile its paradoxical holdings—approving the property tax abatement, yet invalidating the franchise tax credit.

Given the anti-coercion standard’s apparent shortcomings, the question emerges of whether "nondiscrimination," like "obscenity," defies precise constitutional delineation. The answer, indeed, may be yes; however, this does not mean that state and local government is without any constitutional guidance with respect to the exercise of the taxation power. Recent Commerce Clause jurisprudence suggests that state and local governments' ability to affect interstate commerce through taxation expands well-beyond the strictures of Cuno.

In Camps Newfound/Owatonna, Inc. v. Town of Harrison, the Supreme Court invalidated a Maine property tax exemption, rejecting the argument that

lower taxation in State A or State B.

116. Cuno, 386 F.3d at 746.

117. See id. at 743-46. Literally applied, Cuno could invalidate the full gamut of state and local taxation, from location incentives (such as Ohio's franchise tax credit) to sales and use taxes—after all, if a state offers a comparatively law sales and use tax, the decreased tax burden could arguably coerce business decisions, creating a distinct commercial advantage for local industry within the taxing state. See Zelinsky, supra note 97, at 72-73.

118. See Cuno, 386 F.3d at 750; see also Zelinsky, supra note 97, at 75 (expressing skepticism that "some tax policies should be condemned as coercive when the economic substance of those policies is . . . identical to the substance of tax policies which pass the coercion test"). The property tax credit, arguably, applies with the same coercive force as the investment tax credit if comparing similarly situated entities (e.g., two out-of-state businesses). If, indeed, "humans respond to incentives," lower property taxes in one state versus another would affect investment-related location decisions. See Levitt & Dubner, supra note 1, at 7.

119. See Jacobellis v. Ohio, 378 U.S. 184, 197 (1964) (Stewart, J., concurring) (defining "obscenity" as "I know it when I see it").

120. See Zelinsky, supra note 97, at 79-88 (arguing that the ill-defined nondiscrimination factor is inherently flawed, requiring abandonment).

121. 520 U.S. 564 (1997).
the provision somehow did not implicate interstate commerce. Even though Camps Newfound/Owatonna’s business was principally local (its product was delivered and consumed in-state), the Court concluded that the summer camp “unquestionably engaged in interstate commerce.” The Court grounded its decision in the contemporary relationship between the Commerce Clause and its negative corollary: “the definition of ‘commerce’ is the same when relied on to strike down or restrict state legislation as when relied on to support some exertion of federal control or regulation.”

Under the often-expansive definition of “commerce” employed by the Supreme Court in congressional regulation cases, few state and local taxation schemes appear immune from constitutional scrutiny. Tax-based location incentives, however, may present the exceptional case. As the Court reiterated in United States v. Lopez, “the power to regulate commerce, though broad indeed, has limits.”

The Supreme Court held in Lopez that Congress exceeded its authority under the Commerce Clause when it enacted legislation prohibiting the possession of firearms in local school zones. To hold otherwise, the Court explained, would suggest “that there never will be a distinction between what is truly national and what is truly local.” Justice Kennedy, in concurrence, emphasized the degree in which the challenged congressional statute impacted federalism:

The statute now before us forecloses the States from experimenting and exercising their own judgment in an area

122. Id at 572-76, 595.
123. Id. at 573. The Supreme Court analogized the summer camp’s business “to hotels that offer their guests goods and services that are consumed locally.” See id. In both instances, if official discrimination (tax or otherwise) limits nonresidents’ access, “interstate commerce . . . feels the pinch.” See id. (quoting Heart of Atlanta Motel, Inc. v. United States, 379 U.S. 241, 258 (1964)).
124. Id. at 574 (quoting Hughes v. Oklahoma, 441 U.S. 322, 326 n.2 (1979)).
126. See JEROME Hellerstein & WALTER Hellerstein, State Taxation pt. 4.05 (3d ed. 2005).
128. Id. at 558 (quoting Maryland v. Wirtz, 392 U.S. 183, 196 (1968)).
129. See Lopez, 514 U.S. at 567-68.
130. Id. at 568-69. Five years later, the Supreme Court echoed this language when it rebuked the notion that the Commerce Clause granted Congress the authority to enact legislation affording victims of gender-motivated violence a federal civil remedy. See United States v. Morrison, 529 U.S. 598, 617-18 (2000) (“The Constitution requires a distinction between what is truly national and what is truly local.”).
to which States lay claim by right of history and expertise, and it does so by regulating an activity beyond the realm of commerce in the ordinary and usual sense of that term. The tendency of the statute to displace state regulation in areas of traditional state concern is evident from its territorial operation.\textsuperscript{131} The congressional regulation in \textit{Lopez}, therefore, did not warrant Commerce Clause scrutiny because the connection between the challenged statute and the normal conceptions of the term “commerce” was so attenuated.\textsuperscript{132}

\textit{Camps Newfound/Owatonna} and \textit{Lopez} together suggest that the application of the negative Commerce Clause necessarily depends on whether interstate “commerce,” in fact, has been implicated. Given that “the same interstate attributes that establish Congress’s power to regulate commerce also support constitutional limitations on the powers of the States,”\textsuperscript{133} absent these interstate attributes, state and local government would appear to have wide-latitude to experiment with taxation measures. So far, however, this contention lacks real world support.\textsuperscript{134} Even so, certain state and local tax provisions arguably are “truly local,”\textsuperscript{135} which warrants the question of whether such provisions are subject to constitutional scrutiny in the first instant.\textsuperscript{136}

\textbf{D. The Case for Location Incentives}

Location incentives do not meet the threshold “commerce” requirement articulated by the Supreme Court;\textsuperscript{137} thus such incentives should be immune from negative Commerce Clause scrutiny. First, location incentives are truly local in nature. Unlike the protectionist tax measures that ran afoul of the

\textsuperscript{131} \textit{Lopez}, 514 U.S. at 583 (Kennedy, J., concurring).

\textsuperscript{132} \textit{See id.} at 568; \textit{see also} Hellerstein \& Hellerstein, \textit{supra} note 126, at pt. 4.05.

\textsuperscript{133} Hellerstein \& Hellerstein, \textit{supra} note 126, at pt. 4.05 (quoting Lewis v. BT Inv. Managers, Inc., 447 U.S. 27, 39 (1980)).

\textsuperscript{134} \textit{See Hellerstein \& Hellerstein, supra} note 126, at pt. 4.05 & n.72 (citing state and local tax case law in which claims of discriminatory taxation were held not to involve “interstate commerce” and, therefore, were not cognizable under the Commerce Clause).

\textsuperscript{135} \textit{See Lopez}, 514 U.S. at 568-69; \textit{Compare Am. Trucking Ass'ns, Inc. v. Michigan Public Serv. Comm'n}, 125 S. Ct. 2419 (2000), in which the Supreme Court held that Michigan’s $100 annual assessment on trucks engaged in intrastate commerce did not violate the negative Commerce Clause: “Nothing in our case law suggests that such a neutrally, locally-focused fee or tax is inconsistent with the dormant Commerce Clause.” \textit{See id.} at 2423 (emphasis added).

\textsuperscript{136} \textit{See Hellerstein \& Hellerstein, supra} note 126, at pt. 4.05.

\textsuperscript{137} \textit{See supra} notes 127-33 and accompanying text.
negative Commerce Clause in the Supreme Court's nondiscrimination cases, location incentives—in purpose and effect—operate akin to subsidies. As such, location incentives cannot be said to burden interstate commerce, generally. Instead location incentives are more analogous to state and local "laws [enacted] pursuant to . . . police powers that have the purpose and effect of encouraging domestic industry." And, "[n]o one disputes that a State may [such] enact laws."

Judicial invalidation of location incentives, secondly, may inhibit both the ability of sub-national government to experiment effectively with local tax structures and the free exercise of independent judgment regarding local economic policy. This represents the antithesis of the shared, federal system of government contemplated by the Framers. To be sure, judicially imposed limits on state and local economic experimentation may risk "serious consequences for the nation." To this point, Justice Brandies noted nearly a century ago that "[i]t is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel . . . economic experiments without risk to the rest of the country."

138. See, e.g., Boston Stock Exch., 429 U.S. at 337 (invalidating securities tax credit available for securities transactions completed in-state, yet denied if the identical transaction was completed out-of-state); Westinghouse Elec. Corp., 466 U.S. at 401 (striking down import tax allocated in inverse proportion to the ratio of business conducted in-state).

139. See generally Zelinsky, supra note 97 (arguing that there is no rational distinction between state and local taxation versus subsidization).

140. See New Energy Co. of Ind., 486 U.S. at 278 (observing that "direct subsidization of domestic industry ordinarily does not run afoul of th[e] prohibition [against] . . . discriminatory taxation").

141. Bacchus Imps. Ltd., 468 U.S. at 271. Location incentives (like Ohio's franchise tax credit) are more akin to land use legislation such as tax increment financing. In purpose and effect, location incentives merely decrease the economic burden a business incurs within the taxing state, but without the concomitant increase in the burden of transacting business out-of-state, unless economic competition among states is presumed to be a zero-sum game. But cf. Cuno, 386 F.3d at 745, 746 (finding that Ohio's franchise tax credit "encourage[d] further investment in-state at the expense of development in other states").

142. Bacchus Imps., Ltd., 468 U.S. at 271.

143. Adele Nicholas, Supreme Court to Evaluate State Tax Incentives, CORPORATE LEGAL TIMES, Dec. 2006, at 60 ("Our system has always allowed states to experiment with tax incentives as long as they don't interfere with interstate commerce. If the Supreme Court invalidates this incentive, there will be a tremendous amount of chaos.").

144. Cf. Lopez, 514 U.S. at 583.


146. Id. Indeed, purposeful experimentation is a hallmark of the federal system, allowing sub-national government to address peculiar needs:

Viewed as a whole, [the Supreme Court's] jurisprudence has recognized that the needs of society have varied between different parts of the Nation, just as they
Finally, it is a traditional concern of state and local government to encourage local economic growth and development. This role stems from the well-established notion that “State[s] may . . . compete with other States for a share of interstate commerce.” The Supreme Court explicitly has recognized this traditional role in each of its nondiscrimination cases under the negative Commerce Clause.

To conclude that location incentives implicate interstate “commerce in the ordinary and usual sense of that term” strains the imagination. Location incentives typically operate—in purpose and effect—like subsidies, not tariffs. Furthermore, principles of federalism and the traditional role of state and local governments in fostering economic growth and development strongly suggest that, to the extent that location incentives are “commerce,” the term’s usage is in a truly local sense.

V. CONCLUSION

Location incentives will continue to be an important tool in sub-national economic development whether in the form of taxation or subsidies. Similar to economists, state and local legislators “love to dream up and enact them, study them and tinker with them.” Although Supreme Court recognition of the constitutionality of this form of local economic experimentation is longstanding, recent case law and legal commentary suggest otherwise; that

have evolved over time in response to changed circumstances . . . . [The Court’s] earliest cases in particular embodied a strong theme of federalism, emphasizing the “great respect” that we owe to state legislatures . . . in discerning local needs.


147. See supra Part II.
149. See Westinghouse Elec. Corp., 466 U.S. at 406 n.12; see also Bacchus Imps., Ltd., 468 U.S. at 271.
150. Lopez, 514 U.S. at 583 (Kennedy, J., concurring).
151. See generally Zelinsky, supra note 97.
152. See supra note 141 and accompanying text. Similar to the constitutionally permissible provision in Am. Trucking Ass'ns, Inc., 125 S. Ct. at 2426, location incentives, such as the challenged provision in Cuno, credit “only . . . intrastate transactions—that is, . . . activities taking place exclusively within the State's borders.” Id. at 2423. It is debatable whether the states’ offer of location incentives somehow represents a “prisoner dilemma,” “jeopardizing the welfare of the Nation as a whole.” See id. (quoting Oklahoma Tax Comm’n v. Jefferson Lines, Inc., 514 U.S. 175, 180 (1995)); cf. Paul E. McGreal, The Flawed Economics of the Dormant Commerce Clause, 39 WM. & MARY L. REV. 1191, 1273-87 (1998) (arguing that negative Commerce Clause scrutiny is actually the cause not the symptom of the states' economically destructive prisoner's dilemma).
153. LEVITT & DUBNER, supra note 1, at 13.
certain tax-based incentives violate the nondiscrimination requirement of the negative Commerce Clause by coercing business location decisions. Even so, with some state and local taxation, "any 'effect ... on interstate commerce is incidental,' rendering ... claim[s] of discrimination 'a matter of pure speculation."'\(^{154}\) While the negative Commerce Clause shields against states' "tendencies toward economic Balkanization,"\(^{155}\) it cannot be said to proscribe neutral taxation of "purely local activity."\(^{156}\) Location incentives, typically, are "neutral, locally focused" taxation provisions.\(^{157}\) Accordingly, location incentives do not implicate the negative Commerce Clause.

BOOKER T. COLEMAN, JR.


156. See *Am. Trucking Ass'ns, Inc.*, 125 S. Ct. at 2423; *cf.* United States v. Morrison, 529 U.S. 598, 617-18 (2000) ("The Constitution requires a distinction between what is truly national and what is truly local."). This is not to suggest that the constitutional analysis of location incentives should somehow turn on the distinction between "national" versus "local" matters, long rejected in congressional regulation cases. See *United States v. Darby*, 312 U.S. 100, 117-18 (1941). Rather location incentives that are equally apportioned and targeted toward local growth and development will not result in the type of sub-national economic retaliation which concerned the Framers. See *Hughes*, 441 U.S. at 325.

157. *Id.* at 2423 ("Nothing in our case law suggests that such a neutral, locally focused fee or tax is inconsistent with the dormant Commerce Clause.").