THE DORMANT COMMERCE CLAUSE: ECONOMIC DEVELOPMENT IN THE WAKE OF *CUNO*

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INTRODUCTION

Economic development has been in the forefront of the news for many years. As industries have folded, states have scrambled to bring in new businesses or help other businesses within their state expand so that jobs will not be lost. At times, states are in direct competition with one another as each tries to put together the best incentive package to attract jobs. To attract prospective businesses, such packages might include incentives such as tax credits, refunds, or abatements from a variety of state taxes; direct subsidies which can take the form of cash and land grants; low-interest loans and financing; or preferential government purchasing practices.[1] These "bidding wars" between the states have become commonplace.[2]

The use of state tax policy to shape a state's economic development is not new. In the early development of our nation, taxes were unsuccessfully used as obstacles to prevent out-of-state businesses from competing with local companies.[3] However, in recent years, tax incentives have been used to influence businesses to decide where to locate.[4] These tax incentives have recently been challenged as discriminating against interstate commerce by a group of citizens and businesses in Ohio that were displaced when DaimlerChrysler received incentives to construct a new Jeep plant in Toledo.[5]

The Commerce Clause has been interpreted not only to confer power on Congress to regulate commerce, but also to limit the states' power to interfere

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1. Matthew Schaefer, *State Investment Attraction Subsidy Wars Resulting from a Prisoner's Dilemma: The Inadequacy of State Constitutional Solutions and the Appropriateness of a Federal Legislative Response*, 28 N.M. L. REV. 303, 306-07 (1998).

2. Peter D. Enrich, *Saving the States from Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 380 (1996).

3. *See* Guy v. Baltimore, 100 U.S. 434, 443-44 (1879) (holding unconstitutional a statute that required vessels to pay wharfage fees if transporting products not from the state of Maryland); Welton v. Missouri, 91 U.S. 275, 282 (1875) (holding unconstitutional a statute that required itinerant salesmen to purchase a license if selling goods produced out-of-state); Brown v. Maryland, 25 U.S. 419, 449 (1827) (holding unconstitutional a statute that required importers of out-of-state articles to purchase a license before being permitted to sell such articles).

4. Walter Hellerstein, *Commerce Clause Restraints on State Tax Incentives*, 82 MINN. L. REV. 413, 413 (1997); William J. Barrett VII, Note, *Problems with State Aid to New or Expanding Businesses*, 58 S. CAL. L. REV. 1019, 1023-24 (1985).

5. *Court Ruling Jeopardizes Ohio Projects*, TOL. BUS. J., Oct. 1, 2004, at 1.

with commerce.[6] However, the Supreme Court indicated in *Boston Stock Exchange v. State Tax Commission*[7] that the Commerce Clause "does not prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry."[8] Nor does it prevent competition between the states for a share of interstate commerce as long as "no state . . . discriminatorily tax[es] the products manufactured or the business operations performed in any other State."[9] The father of our Constitution, James Madison, wrote:

> [T]he Commerce Clause "grew out of the abuse of the power by the importing States in taxing the non-importing, and was intended as a negative and preventive provision against injustice among the States themselves, rather than as a power to be used for the positive purposes of the General Government."[10]

The Supreme Court has not yet weighed in on the constitutionality of economic development incentive packages, though its prior decisions related to tax incentives provide some guidance. "The Supreme Court has repeatedly invoked the Commerce Clause to condemn state tax measures that protect in-state businesses from out-of-state rivals"[11] or "that impose special burdens that deter out-of-state businesses from competing for business in the state."[12] Nevertheless, in reviewing the Court's prior precedent, "it sometimes is difficult to distinguish a tax that legitimately 'encourag[es] the growth and development of intrastate commerce and industry' from a tax that unconstitutionally discriminates against interstate commerce."[13]

Even though the Court has not addressed a challenge assessing whether "a state tax provision's primary purpose or effect is to attract business to locate or expand in the state,"[14] the United States Court of Appeals for the Sixth Circuit was given that opportunity when it held in *Cuno v. DaimlerChrysler, Inc.* that the investment tax credit granted by Ohio to DaimlerChrysler to build its new Jeep

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6. Philip M. Tatarowicz & Rebecca F. Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 VAND. L. REV. 879, 881 (1986).

7. 429 U.S. 318 (1977).

8. *Id.* at 336.

9. *Id.* at 336-37.

10. West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 193 n.9 (1994) (quoting 3 M. FARRAND, RECORDS OF THE FEDERAL CONVENTION OF 1787, at 478 (1911)).

11. Enrich, *supra* note 2, at 381 (citing *West Lynn Creamery*, 512 U.S. at 188; Bacchus Imports, Ltd. v. Dias, 468 U.S. 263, 276 (1984); Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336 (1977)).

12. *Id.* (citing New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 280 (1988); American Trucking Ass'ns v. Scheiner, 483 U.S. 266, 296-97 (1987); Armco Inc. v. Hardesty, 467 U.S. 638, 642-44 (1984)).

13. Tatarowicz & Mims-Velarde, *supra* note 6, at 885 (quoting Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336 (1977)).

14. Enrich, *supra* note 2, at 381.

plant in Toledo violated the Commerce Clause.[15]

Additionally, there has been considerable debate over the effectiveness and wisdom of state tax and business incentives.[16] Some scholars argue that the use of state tax incentives creates a "prisoners' dilemma"[17] or "race to the bottom"[18] resulting in an adverse fiscal impact.[19] Others cast a skeptical look at those arguments and contend that "competition among states for business may actually facilitate the objective created by the Commerce Clause of achieving economic integration for the benefit of the nation as a whole."[20] The purpose of this Note is not to enter this debate but to analyze various tax incentives employed by the states to induce businesses to locate or expand within their borders. This analysis evaluates the reasoning employed by the Sixth Circuit in its recent decision of *Cuno v. DaimlerChrysler*.[21]

Part I of this Note briefly examines previous United States Supreme Court decisions regarding dormant Commerce Clause issues. Part II specifically analyzes the Ohio economic development incentive package recently provided by the City of Toledo to DaimlerChrysler to construct a new vehicle-assembly plant. The Sixth Circuit concluded that a portion of the package, specifically, the "investment tax credit [could] not be upheld under the Commerce Clause of the United States Constitution."[22] The personal property tax exemption, however, was upheld.[23] This decision places the states in the Sixth Circuit at a much greater disadvantage in attracting business to their states. Rather than removing barriers to interstate commerce, it seems that the court has instead put them in place. In Part III, this Note compares the *Cuno* decision of the Sixth Circuit to a Michigan Supreme Court decision which upheld the validity of a capital acquisition deduction that was, in relevant part, identical to the Ohio investment

15. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 746 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704).

16. Hellerstein, *supra* note 4, at 413.

17. *See generally* Schaefer, *supra* note 1, at 342 (concluding "[e]ach state would be better off if its ability to grant investment attraction subsidies was limited[,]" though no state "wants to unilaterally disarm" and incur the result).

18. Enrich, *supra* note 2, at 380. *But cf.* Richard L. Revesz, *Rehabilitating Interstate Competition: Rethinking the "Race-to-the-Bottom" Rationale for Federal Environmental Regulation*, 67 N.Y.U. L. REV. 1210, 1236-42 (1992).

19. James R. Rogers, *The Effectiveness and Constitutionality of State Tax Incentive Policies for Locating Business: A Simple Game Theoretic Analysis*, 53 TAX LAW. 431, 431 (2000).

20. Clayton P. Gillette, *Business Incentives, Interstate Competition, and the Commerce Clause*, 82 MINN. L. REV. 447, 448 (1997); *see also* Daniel P. Petrov, Note, *Prisoners No More: State Investment Relocation Incentives and the Prisoners' Dilemma*, 33 CASE W. RES. J. INT'L L. 71, 104-10 (2001) (contending that the prisoners' dilemma must be adjusted for complexities and justifications for relocation incentives).

21. 386 F.3d 738, 742-48 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704).

22. *Id.* at 746.

23. *Id.* at 748.

tax credit.

Part IV of this Note evaluates how other economic development tax incentives, including subsidies, fare based on the broad interpretation by the Sixth Circuit of tax incentives that burden interstate commerce. Notwithstanding the broad interpretation by the Sixth Circuit, many of these incentives should still pass constitutional scrutiny. Finally, the conclusion of this Note addresses which state tax incentives, if challenged, should be upheld and why.

I. Dormant Commerce Clause Cases

The Commerce Clause of the United States Constitution provides in part that "Congress shall have Power . . . [t]o regulate [c]ommerce . . . among the several States . . . ."[24] Thus, the Constitution explicitly gives Congress the power to regulate commerce between states.

Even though the Commerce Clause is phrased as a grant of regulatory power, Justice Scalia noted in *New Energy Co. of Indiana v. Limbach*[25] that it has long been accepted that the Commerce Clause also directly limits the power of the States to discriminate against interstate commerce and "[t]hus, state statutes that clearly discriminate against interstate commerce are routinely struck down."[26] This "negative" aspect is also referred to as the "dormant" Commerce Clause.[27] "The policy behind this doctrine is simple: to prevent the states—in the absence of congressional action—from creating insurmountable barriers among themselves, thereby eradicating the unity that the Framers of our Constitution strove to create."[28] Justice Cardozo noted that "[the Constitution] was framed upon the theory that the peoples of the several states must sink or swim together, and that in the long run prosperity and salvation are in union and not division."[29] Following is a summary of recent cases decided by the Court in which state taxes raised a dormant Commerce Clause issue.

A. Boston Stock Exchange v. State Tax Commission

In *Boston Stock Exchange v. State Tax Commission*,[30] the Court struck down a New York statute that imposed a higher tax on transfers of stock that occurred outside the state than on transfers which involved a sale within the state.[31] The Court noted that "[t]he obvious effect of the tax [was] to extend a financial advantage to sales on the New York exchanges at the expense of the regional

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24. U.S. CONST. art. I, § 8, cl. 3.

25. 486 U.S. 269 (1988).

26. *Id.* at 274.

27. Tatarowicz & Mims-Velarde, *supra* note 6, at 881-82.

28. Amy M. Petragnani, *The Dormant Commerce Clause: On Its Last Leg*, 57 ALB. L. REV. 1215, 1215 (1994).

29. Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336 n.14 (1977) (quoting Baldwin v. G.A.F. Seelig, Inc., 294 U.S. 511, 522-23 (1935)).

30. 429 U.S. 318 (1977).

31. *Id.* at 328 (referencing N.Y. TAX LAW § 270-a (McKinney Supp. 1976)).

exchanges."[32]

B. Maryland v. Louisiana

In *Maryland v. Louisiana*,[33] the Court exercised original jurisdiction in an action by "several States, joined by the United States and a number of pipeline companies, challeng[ing] the constitutionality of Louisiana's 'First-Use Tax' imposed on certain uses of natural gas brought into Louisiana, principally from the Outer Continental Shelf (OCS)."[34] The statute,[35] along with other state statutes,[36] provided a number of exemptions and credits related to the tax. The net effect, for the most part, was that Louisiana consumers of OCS gas were not burdened by the tax, but the tax did apply to gas moving out of state. The Court thus concluded that "the First-Use Tax [was] unconstitutional under the Commerce Clause because it unfairly discriminate[d] against purchasers of gas moving through Louisiana in interstate commerce."[37]

C. Westinghouse Electric Corp. v. Tully

In *Westinghouse Electric Corp. v. Tully*,[38] the New York statute at issue was in response to federal Domestic International Sales Corporation ("DISC") legislation.[39] A state franchise tax provision allowed certain businesses an income tax credit based on the portion of the business's exports shipped from locations within New York.[40] The Court provided detailed examples of how the credit was designed to increase as New York's share of the export activity increased and therefore decreased as the other states' export activity increased.[41] The intended purpose of the credit was to "ensure that New York would not lose its competitive position vis-a-vis other States, since other States were also expected to offer tax benefits to DISCs."[42] The Court concluded that not only did the New York tax scheme provide a positive incentive for increased export activity in New York,[43] but it also penalized increases in DISC's shipping activities in other states and therefore was in violation of the Commerce Clause.[44]

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32. *Id.* at 331.
33. 451 U.S. 725 (1981).
34. *Id.* at 728.
35. LA. REV. STAT. ANN. §§ 47:1301-47:1307 (West Supp. 1981).
36. *Id.* § 47:647.
37. *Maryland v. Louisiana*, 451 U.S. at 760.
38. 466 U.S. 388 (1984).
39. *Id.* at 393 (referencing N.Y. TAX LAW §§ 208-219-a (McKinney Supp. 1983-1984)).
40. *Id.*
41. *Id.* at 401 n.9.
42. *Id.* at 397.
43. *Id.* at 400-01.
44. *Id.* at 407.

D. Bacchus Imports, Ltd. v. Dias

In *Bacchus Imports, Ltd. v. Dias*,[45] Hawaii imposed a twenty percent excise tax on sales of liquor at wholesale. However, an exemption was allowed for fruit wine manufactured in Hawaii and for okolehao, a brandy distilled from the root of a shrub indigenous to Hawaii.[46] The Court noted that "[a] finding that state legislation constitutes 'economic protectionism' may be made on the basis of either discriminatory purpose . . . or discriminatory effect."[47] The Court concluded that the Hawaii liquor tax exemption "violated the Commerce Clause because it had both the purpose and effect of discriminating in favor of local products."[48]

E. New Energy Co. of Indiana v. Limbach

New Energy Co. of Indiana v. Limbach[49] involved an Ohio tax credit designed to encourage the in-state production of ethanol. Ohio allowed a tax credit against the state's motor fuel tax for each gallon of ethanol sold by fuel dealers, but only if the ethanol was produced in Ohio or in a state that granted similar tax advantages to ethanol produced in Ohio.[50] The Court concluded that the provision "explicitly deprive[d] certain products of generally available beneficial tax treatment because they [were] made in certain other States, and thus on its face appear[ed] to violate the cardinal requirement of nondiscrimination."[51]

F. West Lynn Creamery, Inc. v. Healy

In *West Lynn Creamery, Inc. v. Healy*,[52] "a Massachusetts pricing order impose[d] an assessment on all fluid milk sold by dealers to Massachusetts retailers."[53] Approximately two-thirds of that milk was produced out-of-state; however, "the entire assessment . . . [was] distributed to Massachusetts dairy farmers."[54] The state argued that "[b]ecause each component of the program—a local subsidy and a nondiscriminatory tax—[was] valid, the combination of the two [would be] equally valid."[55]

The Court noted that even if both components of the pricing order were valid,

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45. 468 U.S. 263 (1984).
46. *Id.* at 265; *see* HAW. REV. STAT. § 244-4(6), (7) (Supp. 1983).
47. *Bacchus Imports, Ltd.*, 468 U.S. at 270 (citations omitted).
48. *Id.* at 273.
49. 486 U.S. 269 (1988).
50. *Id.* at 272; *see* OHIO REV. CODE ANN. § 5735.145(B) (West 1986).
51. *New Energy Co. of Ind.*, 486 U.S. at 274.
52. 512 U.S. 186 (1994).
53. *Id.* at 188.
54. *Id.*
55. *Id.* at 198.

the pricing statute was nevertheless unconstitutional.[56] Justice Stevens, speaking for the majority, stated that "[a] pure subsidy funded out of general revenue ordinarily imposes no burden on interstate commerce, but merely assists local business."[57] Generally, "[t]he existence of major in-state interests adversely affected . . . is a powerful safeguard against legislative abuse."[58] In this case, however, the pricing order was funded principally from taxes on the sale of milk produced in other states. By funding the subsidy in this manner, the Court noted that the state not only assisted local farmers, but also burdened interstate commerce by "violat[ing] the cardinal principle that a State may not 'benefit in-state economic interests by burdening out-of-state competitors.'"[59]

II. RECENT DECISIONS AFFECTING ECONOMIC DEVELOPMENT

The Commerce Clause has been cited repeatedly by the Supreme Court to condemn state tax measures that protect in-state businesses from out-of-state rivals[60] or that impose special burdens on out-of-state businesses in order to deter them from competing for business in-state.[61] Even though the Court has not addressed "a challenge [where the] state tax provision's primary purpose or effect is to attract businesses to locate or expand in the state,"[62] the United States Court of Appeals for the Sixth Circuit did address this challenge in *Cuno v. DaimlerChrysler*.[63] However, hopefully the murky waters of the dormant Commerce Clause will become much clearer as the Court has granted certiorari to the *Cuno* appellants.[64]

A. Cuno v. DaimlerChrysler, Inc.

In 1998, DaimlerChrysler, Inc., in exchange for various tax incentives, entered into an agreement with the City of Toledo to construct a new vehicle-assembly plant near the company's existing facility. These incentives included a 100% property tax exemption as well as an investment tax credit of 13.5 % against the state corporate franchise tax for certain qualifying investments. Ohio's investment tax credit grants a taxpayer a nonrefundable

56. *Id.* at 199.

57. *Id.*

58. *Id.* at 200 (quoting Minnesota v. Clover Leaf Creamery Co., 449 U.S. 456, 473 n.17 (1981)).

59. *Id.* at 199 (quoting New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 273-74 (1988)).

60. Enrich, *supra* note 2, at 381 (citing *West Lynn Creamery*, 512 U.S. at 188; Bacchus Imports, Ltd. v. Dias, 468 U.S. 263, 276 (1984); Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336 (1977)).

61. *Id.* (citing *New Energy Co. of Ind.*, 486 U.S. at 280; Am. Trucking Ass'ns v. Scheiner, 483 U.S. 266, 296-97 (1987); Armco Inc. v. Hardesty, 467 U.S. 638, 642-44 (1984)).

62. *Id.*

63. 386 F.3d 738 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704).

64. *Id.*

credit against the state's corporate franchise tax if the taxpayer "purchases new manufacturing machinery and equipment during the qualifying period, provided that the new manufacturing machinery and equipment are installed in [Ohio]."[65] The court of appeals determined this to be in violation of the Commerce Clause.[66] The property tax exemption, however, was upheld.[67]

The parties did not dispute that "the tax provisions at issue [had] a sufficient nexus with the state, [were] fairly apportioned, and [were] related to benefits provided by the state."[68] Likewise, the parties did not dispute that "it [was] legitimate for Ohio to structure its tax system to encourage new intrastate economic activity."[69] The plaintiffs in *Cuno*, however, maintained that even though the investment tax credit at issue was equally available to in-state and out-of-state businesses, the state's investment tax credit "coerc[ed] businesses already subject to the Ohio franchise tax to expand locally rather than out-of-state."[70]

Specifically, the plaintiffs noted that by locating significant new machinery and equipment within the state any corporation doing business within the state of Ohio, and thus paying the state's corporate franchise tax, could reduce its existing tax liability.[71] The corporation, however, would not receive a reduction in its corporate franchise tax liability if a comparable plant and equipment were located elsewhere.[72] The plaintiffs noted that as a result, two businesses similarly situated and each subject to Ohio taxation would be treated differently. Namely, the business that made a choice to expand its presence in Ohio would receive a reduced tax burden, based directly on its new in-state investment, whereas a competitor that invested out-of-state would face a comparatively higher tax burden because it would be ineligible for any credit against its Ohio tax.[73]

The plaintiffs analogized the Ohio investment tax credit to the tax provisions

65. OHIO REV. CODE ANN. § 5733.33(B)(1) (West 2004). The investment tax credit is generally 7.5 percent "of the excess of the cost of the new manufacturing machinery and equipment purchased during the calendar year for use in a county over the county average new manufacturing machinery and equipment investment for [the] county." *Id.* § 5733.33(C)(1). The rate increases to 13.5 percent of the cost of the new investment if it is purchased for use in specific economically depressed areas. *Id.* § 5733.33(C)(2), (A)(8)-(13).

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

67. *Id.* at 748.

68. *Id.* at 742; *see also* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977) (referring to the four concrete concerns identified by the Court that a state tax provision must satisfy in order to pass constitutional muster). Specifically, a tax will be upheld against a Commerce Clause challenge "when the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." *Id.*

69. *Cuno*, 386 F.3d at 742.

70. *Id.* at 743.

71. *Id.*

72. *Id.*

73. *Id.*

considered in *Boston Stock Exchange*, *Maryland v. Louisiana*, and *Westinghouse Electric Corp.*, arguing that Ohio encouraged the development of local business though its "power to tax an in-state operation as a means of 'requiring [other] business operations to be performed in the home State.'"[74] The plaintiffs further contended that the Ohio investment tax credit, like the tax credit in *Maryland v. Louisiana*, encouraged further investment in-state at the expense of development in other states which in turn hindered free trade among the states.[75]

The defendants argued that "the Supreme Court's opinions 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."[76] The defendants cited the theory espoused by Philip Tatarowicz and Rebecca Mims-Velarde who have concluded that "a state tax incentive that focuses exclusively on a taxpayer's in-state activities does not have the sort of negative impact on interstate commerce with which the [C]ommerce [C]lause is concerned."[77] Instead, Tatarowicz and Mims-Velarde suggested that "the 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 [as well as] out-of-state activities in determining the taxpayer's effective tax rate."[78] The court commented that based on Tatarowicz's and Mims-Velarde's view, "the Commerce Clause is primarily concerned with preventing economic protectionism—that is, regulatory measures designed to benefit local interests by burdening out-of-state commerce."[79]

The court agreed that it was "arguably possible" to fit the Supreme Court cases into the framework suggested by Tatarowicz and Mims-Velarde but determined it "clear" that "the Court itself has not adopted this approach in analyzing dormant Commerce Clause cases."[80] The court cited *Bacchus Imports, Ltd.* and *Westinghouse Electric Corp.* in reaching this conclusion; however, it did not discuss how the cases were analogous. In *Westinghouse*, New York allowed certain businesses an income tax credit based on the portion of the business's exports shipped from New York.[81] In *Bacchus*, Hawaii allowed an exemption from its excise tax on sales of liquor at wholesale for fruit wine manufactured in Hawaii.[82] Both those cases involved the sale of goods and a continuing benefit to in-state economic activity at the expense of out-of state activity, whereas the tax credit at issue in *Cuno* relates not to the sale of goods in interstate commerce but to a one time reduction in franchise taxes for purchases of new machinery and equipment installed in-state.

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74. *Id.* at 745 (quoting Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336 (1977) (internal citations omitted)).

75. *Id.*

76. *Id.*

77. Tatarowicz & Mims-Velarde, *supra* note 6, at 928-29.

78. *Id.* at 929.

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

80. *Id.*

81. Westinghouse Elec. Corp. v. Tully, 466 U.S. 388, 393 (1984).

82. Bacchus Imports, Ltd. v. Dias, 468 U.S. 263, 265 (1984).

The defendants also argued that the investment tax credit was similar to a direct subsidy; however, this argument was rejected by the court even though it agreed that the two would have the same economic effect.[83] The court stated that "the distinction between a subsidy and a tax credit, in the constitutional sense, results from the fact that the tax credit involves state regulation of interstate commerce through its power to tax."[84]

The Supreme Court has provided that "the first step in analyzing any law subject to judicial scrutiny under the negative Commerce Clause is to determine whether it 'regulates evenhandedly with only 'incidental' effects on interstate commerce, or discriminates against interstate commerce.'"[85] Discrimination in the context of interstate commerce "simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter. If a restriction on commerce is discriminatory, it is virtually *per se* invalid."[86]

However, the Supreme Court indicated in *Boston Stock Exchange* that the Commerce Clause "does not prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry."[87] Nor does it prevent competition between the states for a share of interstate commerce as long as "no State . . . discriminatorily tax[es] the products manufactured or the business operations performed in any other State."[88] Ohio, along with every other state in the nation, has structured its tax system to encourage growth and development. In Ohio, that included an investment tax credit on qualifying purchases of machinery and equipment, yet the Sixth Circuit held that "Ohio's investment tax credit [could not] be upheld under the Commerce Clause of the United States Constitution."[89] Although the court quoted several passages from the previously noted Supreme Court dormant Commerce Clause precedent, it failed to provide an analysis of how *Cuno* was similar to those cases. It simply provided a conclusory statement that Ohio's investment tax credit could not be upheld.[90]

Even though Ohio's investment tax credit was held to violate the dormant Commerce Clause, its personal property tax exemption was upheld.[91] The court distinguished a tax credit from an exemption by explaining that an investment tax credit reduces preexisting income tax liability whereas a personal property exemption does not reduce any preexisting property tax liability but instead "merely allows a taxpayer to avoid tax liability for new personal property put

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

84. *Id.*

85. Or. Waste Sys., Inc. v. Envtl. Quality Comm'n of Or., 511 U.S. 93, 99 (1994) (quoting Hughes v. Oklahoma, 441 U.S. 322, 336 (1979)).

86. *Id.*

87. 429 U.S. 318, 336 (1977).

88. *Id.* at 336-37.

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

90. *Id.*

91. *Id.* at 748.

into first use in conjunction with a qualified new investment."[92] The court went on to state that "the personal property tax exemption is internally consistent because, if universally applied, the new property would escape tax liability irrespective of location."[93] Could not the same be said if the investment tax credit was universally applied?

B. *The Other Side of the Coin*—Caterpillar, Inc. v. Department of Treasury

The decision reached by the Sixth Circuit in *Cuno* was in direct contradiction to the decision reached by the Michigan Supreme Court in *Caterpillar, Inc. v. Department of Treasury*.[94] In *Caterpillar*, the Michigan court upheld a capital acquisition deduction that, although not identical to the Ohio investment tax credit, was similar in that a taxpayer received a higher deduction as more property was located in-state.[95]

Corporations doing business in Michigan pay taxes to the state pursuant to the Single Business Tax Act ("SBT").[96] Before determining its SBT liability, a taxpayer doing business both within and outside of Michigan must apportion its "tax base" by applying a three-factor apportionment formula.[97] This formula (which also was challenged by *Caterpillar*)[98] consists of "the average of three ratios: (1) Michigan payroll to total payroll, (2) Michigan property to total property, and (3) Michigan sales to total sales."[99] After apportionment, the adjusted tax base is subject to additional adjustments including the capital acquisition deduction.[100]

The capital acquisition deduction, just as its name implies, provides a deduction for the acquisition of capital assets.[101] The deduction for the acquisition cost of real property is one hundred percent of the cost of depreciable real property provided that the property is physically located in Michigan.[102] The deduction for tangible personal property, however, is calculated using a two-factor apportionment formula based on the average of payroll and property located in Michigan compared to total payroll and property located everywhere.[103] Caterpillar claimed that the capital acquisition deduction, for both real and tangible personal property, burdened interstate commerce and thus

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92. *Id.* at 747.

93. *Id.* at 748.

94. Caterpillar, Inc. v. Dep't of Treasury, 488 N.W.2d 182, 194 (Mich. 1992).

95. *Id.*

96. *Id.* at 183.

97. *Id.* at 185.

98. *Id.* at 184; *see also* Trinova Corp. v. Mich. Dep't of Treasury, 498 U.S. 358, 387 (1991) (holding the three-factor apportionment formula as applied to the SBT did not violate the Constitution).

99. *Trinova Corp.*, 498 U.S. at 367-68.

100. *Caterpillar*, 488 N.W.2d at 185-86.

101. *Id.* at 186.

102. *Id.* at 187.

103. *Id.* at 186-87.

violated the Commerce Clause of the Constitution.[104]

A majority of the Michigan Supreme Court concluded that the enactment of the capital acquisition deduction was neither for a discriminatory purpose,[105] nor did the capital acquisition deduction have a discriminatory effect.[106] The court determined the two-factor formula utilizing only payroll and property for the deduction related to the acquisition of tangible personal property was fair, as a company's acquisition of capital is most likely to be located where a company's property and employees are located.[107] Similarly, a deduction of the cost of real property located in Michigan was determined to "reasonably reflect[] capital acquisitions related to Michigan business activity."[108] Both Chief Justice Cavanagh[109] and Justice Brickley[110] dissented, claiming that the deduction related to tangible personal property burdened interstate commerce. Justice Brickley, however, disagreed[111] with Justice Cavanagh who concluded that the deduction for the acquisition of real property located in Michigan also discriminated against interstate commerce.[112] Unlike the court majority, both dissenting judges provided a detailed explanation comparing Michigan's capital acquisition deduction to previous Supreme Court Commerce Clause precedent, yet reached different conclusions.

Both dissenting justices compared the personal property deduction to the tax credit on exports disallowed by the Court in *Westinghouse Electric Corp.*[113] In *Westinghouse*, the credit was designed to increase as New York's share of the export activity increased and to decrease as other states' export activity increased.[114] Justice Brickley noted that there was a clear-cut rule emerging from *Westinghouse*: "Basing a deduction on a change in a subset of a company's in-state activity relative to its total activity is unconstitutional."[115] By basing the personal property acquisition deduction on only two of the factors, payroll and property, rather than the three factors used to calculate the apportioned tax base, the capital acquisition deduction is available on different, less favorable, terms to companies depending on the amount of their interstate activities,[116] resulting in the effect condemned in *Westinghouse Electric Corp*.[117] Justice Brickley, however, went on to state that "a deduction apportioned with the same formula

104. *Id.* at 183.
105. *Id.* at 192.
106. *Id.* at 194.
107. *Id.* at 190.
108. *Id.* at 191.
109. *Id.* at 207 (Cavanagh, C.J., dissenting).
110. *Id.* at 216 (Brickley, J., dissenting in part).
111. *Id.* at 219.
112. *Id.* at 208 (Cavanagh, C.J., dissenting).
113. *Id.* at 200-01; *id.* at 216-17 (Brickley, J., dissenting in part).
114. Westinghouse Elec. Corp. v. Tully, 466 U.S. 388, 401 n.9 (1984).
115. *Caterpillar*, 488 N.W.2d at 216 (Brickley, J., dissenting in part).
116. *Id.* at 217.
117. *Id.* at 216 n.6.

as multistate activity generally would reflect the change in the entire activity in Michigan . . . [and] would likely be constitutional."[118]

Unlike Justice Brickley, Chief Justice Cavanagh disagreed with the majority and concluded that the capital acquisition deduction for the cost of depreciable real property located in Michigan was unconstitutional.[119] The Chief Justice concluded that the deduction was facially discriminatory because a company that acquired depreciable real property in Michigan received a deduction, but a company that acquired depreciable real property in another state did not.[120] The discriminatory effect was "to afford an especially preferential tax rate to a Michigan-based company that invests in Michigan, as compared to a non-Michigan based company that invests outside Michigan."[121] Justice Brickley, however, determined that there was no discriminatory effect because the tax was fairly apportioned.[122]

C. *Are* Cuno *and* Caterpillar *Distinguishable?*

Both *Cuno v. DaimlerChrysler* and *Caterpillar, Inc. v. Department of Treasury* involve the acquisition of capital assets. Ohio allows a credit against its corporate franchise tax for qualifying investments of machinery and equipment, provided they are installed in Ohio. Michigan allows a deduction, rather than a credit, for the acquisition of the cost of depreciable real property acquired during the year, provided the property is located in Michigan. The net effect is the same: a lower effective in-state tax rate. The Michigan Supreme Court held that this is not in violation of the Commerce Clause, that the statute allowing it is not facially discriminatory, and that there is neither a discriminatory purpose nor discriminatory effect,[123] yet the Sixth Circuit disagreed.[124]

III. HAS A NAIL BEEN PLACED IN THE COFFIN OF ECONOMIC DEVELOPMENT TAX INCENTIVES? OR JUST WITHIN THE SIXTH CIRCUIT?

Referring to the decisions of the Supreme Court in *Boston Stock Exchange*, *Bacchus Imports, Ltd.*, *Westinghouse Electric Corp.*, and *New Energy Co. of Indiana*, Professor Walter Hellerstein suggests that constitutional suspicion surrounding state tax incentives is well justified.[125] Professors Hellerstein and Coenen commented that "[s]tate tax incentives, whether in the form of credits, exemptions, abatements, or other favorable treatment typically possess two

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118. *Id.*

119. *Id.* at 218.

120. *Id.* at 204 (Cavanagh, C.J., dissenting).

121. *Id.*

122. *Id.* at 220-21 (Brickley, J., dissenting in part).

123. *Id.* at 194 (majority opinion).

124. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 746 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704).

125. Hellerstein, *supra* note 4, at 416.

features that render them suspect under the rule barring taxes that discriminate against interstate commerce."[126] First, they "single out for favorable treatment construction, investments, or other activities that occur within the taxing state."[127] Second, because state tax incentives are "integral components of the state's taxing apparatus," they "are intimately associated with the coercive machinery of the state."[128]

Arguably, a literalistic focus on key passages might suggest that all inducements to encourage new businesses to locate or expand its existing businesses within a state are likely to be unconstitutional.[129] "After all, it is the rare state tax incentive that results in 'tax-neutral decisions' made 'solely on the basis of nontax criteria.'"[130] It thus begs the question: Are all state tax incentives unconstitutional? Instinctively, according to Professor Hellerstein, the answer is no.[131]

The Court itself has stated that the Commerce Clause "does not prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry."[132] Nor does it prevent competition between the states for a share of interstate commerce as long as "no State . . . discriminatorily tax[es] the products manufactured or the business operations performed in any other State."[133] Moreover, "[i]t is a laudatory goal in the design of a tax system to promote investment that will provide jobs and prosperity to the citizens of the taxing State."[134]

Nonetheless, scholars agree that the Supreme Court lacks a clear vision of principles to guide it when deciding Commerce Clause challenges to state taxes.[135] "The Court itself has recognized its lack of consistency."[136] Justice Scalia has described the Court's decisions from the "so-called 'negative'" Commerce Clause as a "quagmire" that makes no sense.[137] Even so, it seems that

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126. Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 793 (1996).

127. *Id.*

128. *Id.* at 794.

129. Hellerstein, *supra* note 4, at 421.

130. *Id.* (quoting Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 331 (1977)).

131. *See id.* at 424.

132. *Boston Stock Exch.*, 429 U.S. at 336.

133. *Id.* at 337.

134. Trinova Corp. v. Mich. Dep't of Treasury, 498 U.S. 358, 385 (1991).

135. 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, 30 (2002) [hereinafter Zelinsky, *Restoring Politics to the Commerce Clause*]; Ferdinand P. Schoettle, *Big Bucks, Cloudy Thinking: Constitutional Challenges to State Taxes—Illumination from the GATT*, 19 VA. TAX REV. 277, 281 (1999); Gillette, *supra* note 20, at 493-94; Walter Hellerstein et al., *Commerce Clause Restraints on State Taxation After Jefferson Lines*, 51 TAX L. REV. 47, 50 (1995); Tatarowicz & Mims-Velarde, *supra* note 6, at 888-89.

136. Schoettle, *supra* note 135, at 283.

137. Tyler Pipe Indus., Inc. v. Wash. State Dep't of Revenue, 483 U.S. 232, 259-60 (1987)

the foundation of the dormant Commerce Clause is the prohibition of economic protectionism.[138] The Court emphasized this in *New Energy*: "This 'negative' aspect of the Commerce Clause prohibits economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors."[139]

A. Within the Sixth Circuit

In the three major cases relied upon by the Sixth Circuit in deciding *Cuno* (*Boston Stock Exchange*, *Maryland v. Louisiana*, and *Westinghouse Electric Corp.*), the Court addressed situations where preferential treatment was given to in-state businesses by imposing a higher tax, or lesser credit, on out-of-state goods or services.[140] Such was also the case in *Bacchus Imports, Ltd.*, to which the Sixth Circuit referred.[141] In each of those cases, an in-state economic interest was protected at the expense of an out-of-state business, resulting in an obvious dormant Commerce Clause issue. In *Boston Stock Exchange*, the legislative history actually confirmed that the purpose of the transfer tax was a protectionist measure.[142] Moreover, "then Governor Nelson Rockefeller confirmed that the

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(Scalia, J., dissenting in part).

138. *See* Bacchus Imports, Ltd. v. Dias, 468 U.S. 263, 270-73 (1984); *cf.* Hunt v. Wash. State Apple Adver. Comm'n, 432 U.S. 333, 352-53 (1977) (holding unconstitutional burdens placed on out-of-state apple producers in order to sell within the state); Dean Milk Co. v. City of Madison, Wis., 340 U.S. 349, 354 (1951) (holding unconstitutional a city ordinance that prohibited the sale of milk in the city unless it had been bottled within five miles of the city).

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

140. Westinghouse Elec. Corp. v. Tully, 466 U.S. 388, 393-94 (1984) (enacting a franchise tax credit based on gross receipts from products shipped from a regular place of business within the state); Maryland v. Louisiana, 451 U.S. 725, 756-58 (1981) (protecting Louisiana consumers of OCS gas by only applying a first-use tax to gas moving out of state); Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 319 (1977) (imposing a transfer tax on sale of securities which was higher if sold out-of-state rather than in-state).

141. *Bacchus Imports*, 468 U.S. at 265 (encouraging in-state commerce by allowing an excise tax exemption for fruit wine manufactured in Hawaii and for okolehao, a brandy distilled from the root of a shrub indigenous to Hawaii).

142. New York, since 1905, had imposed a transfer tax on securities transactions if part of the transaction occurred within the state. *Boston Stock Exch.*, 429 U.S. at 319. However, none of the states in which the appellant stock exchanges were located taxed the sale or transfer of securities. *Id.* at 323. In enacting the amendment to § 270, the legislature recognized that:

> [T]he tax on transfers of stock . . . is an important contributing element to the diversion of sales to other areas to the detriment of the economy of the state. . . . [Therefore], [i]n order to encourage the effecting by nonresidents of the state of New York of their sales within the state of New York and the retention within the state of New York of sales involving large blocks of stock, a separate classification of the tax on sales by nonresidents of the state of New York and a maximum tax for certain large block sales are desirable.

purpose of the new law was to 'provide long-term relief from some of the competitive pressures from outside the State.'"[143] As a result, transactions involving out-of-state sales were taxed more heavily than most transactions involving a sale within the state.[144] Likewise, in *Maryland v. Louisiana*, OCS gas was generally consumed in Louisiana without the burden of the first-use tax. Its principal application was to tax gas moving from Louisiana to out of state.[145]

Westinghouse Electric Corp. is most similar to *Cuno* because, like *Cuno*, it involved an income tax credit. However, unlike *Cuno*, the amount of the New York credit depended on both in-state and out-of-state activity. Since the ratio to calculate the credit was based on DISC gross receipts of export property shipped from within New York to total DISC gross receipts derived from the sale of all export property, the New York credit decreased as the percentage of exports outside New York increased.[146] The Court noted that *it was not the provision of the credit* that offended the Commerce Clause, "but the fact that it [was] allowed on an impermissible basis, i.e., the percentage of a specific segment of the corporation's business that [was] conducted in New York."[147] Thus, not only did the New York tax scheme provide a positive incentive for increased business activity in New York, but it also penalized increases in shipping activities in other states.[148] New York's intention, just as in *Boston Stock Exchange*, was to ensure that it did not lose its competitive position to other states, since other states would also be providing tax benefits to DISCs.[149] In doing so, it "violated the prohibition in *Boston Stock Exchange* against using discriminatory state taxes to burden commerce in other States in an attempt to induce 'business operations to be performed in the home State that could more efficiently be performed elsewhere.'"[150] Thus, the Court once again struck down a statute that had economic protectionism as its intention.

Each of those cases relied on by the Sixth Circuit can be distinguished from *Cuno*. First, the Ohio investment tax credit applied only to in-state activities. Like the export credit in *Westinghouse Electric Corp.*, as in-state activity increased (i.e., purchases of new machinery and equipment installed in-state), the Ohio investment tax credit increased as well; however, unlike *Westinghouse*, the credit did not decrease as out-of-state activity increased.[151] The Ohio credit was tied only to machinery and equipment purchases within the state. There was no

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Id. at 326-27 (quoting 1968 N.Y. Laws c. 827, § 1).

143. *Id.* at 327.

144. *Id.* at 319.

145. *Maryland v. Louisiana*, 451 U.S. at 759.

146. Westinghouse Elec. Corp. v. Tully, 466 U.S. 388, 400-01 n.9 (1984) (explaining how the credit was designed to increase as New York's share of the export activity increased and therefore would decrease as the business's other states' export activity increased).

147. *Id.* at 407 n.12.

148. *Id.* at 400-01.

149. *Id.* at 397.

150. *Id.* at 406 (quoting Pike v. Bruce Church, Inc., 397 U.S. 137, 145 (1970)).

151. *See* OHIO REV. CODE. ANN. § 5733.33(A)(8)-(13), (C)(1), (C)(2) (West 2004).

ratio of Ohio purchases of machinery and equipment to total purchases of machinery and equipment, as was the case in *Westinghouse*. This is a "crucial" distinction.[152] Hence, the Ohio investment tax credit provided a positive incentive for increased business activity in Ohio, but it did not penalize businesses that also increased their property presence in other states.[153]

Similarly, the Court noted in *Boston Stock Exchange* that the New York transfer tax created both "an advantage for the exchanges in New York and a discriminatory burden on commerce to its sister states."[154] If, as a result of the sale, the security was to be delivered or transferred to New York, the seller could not escape liability in New York by selling out-of-state, but the liability could be substantially reduced by selling in-state.[155] This seems to be similar to the investment tax credit in *Cuno*. An increase of manufacturing machinery and equipment located in Ohio yielded a credit from the state's franchise tax, resulting in a lower tax,[156] but that is where the similarities end. In *Boston Stock Exchange*, once a decision was made to sell a security with a portion of the transaction occurring in New York, the taxpayer was subject to the New York tax. However, if the sale took place out-of-state, the New York tax was higher. Thus, the amount of the New York tax depended on whether a portion of the transaction occurred out-of-state. There is no corresponding out-of-state transaction related to the Ohio investment tax credit.

Finally, in *Maryland v. Louisiana*, the net effect of the first-use tax, generally, was that Louisiana consumers of OCS gas were not burdened by the tax, but the tax did apply to competitive users in other states.[157] Specifically, as compared to *Cuno*, an owner paying the first-use tax on OCS gas received an equivalent tax credit on any state severance tax owed in connection with the extraction of natural resources within the state.[158] The Court noted that "[t]he obvious economic effect of this Severance Tax Credit [was] to encourage natural gas owners involved in the production of OCS gas to invest in mineral exploration and development within Louisiana rather than to invest in further OCS development or in production in other States."[159]

Again, this seems similar to the investment tax credit in Ohio. By purchasing new machinery and equipment and installing such machinery and equipment in Ohio, the state's franchise tax can be reduced by a percentage of the qualifying investments, thus providing an incentive for further investment in Ohio rather than investing in other states. Yet the distinction here is that the Louisiana credit

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152. Cuno v. DaimlerChrysler, Inc., 154 F. Supp. 2d 1196, 1203 (N.D. Ohio 2001), *rev'd*, 386 F.3d 738 (6th Cir. 2004).

153. *See Westinghouse Elec. Corp.*, 466 U.S. at 400-01.

154. Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 331 (1977).

155. *Id.*

156. Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 741 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704).

157. Maryland v. Louisiana, 451 U.S. 725, 759 (1981).

158. *Id.* at 732.

159. *Id.* at 757.

went to a specific item resulting in a price differential to in-state and out-of-state taxpayers. As a result of the Louisiana Severance Tax Credit, the price of natural gas to in-state consumers was less than the same product used by out-of-state consumers. There is no similar product correlation related to the Ohio investment tax credit. Out-of-state taxpayers are not required to pay a higher tax on the same item used by an in-state taxpayer in Ohio as a result of the investment tax credit. Thus, out-of-state taxpayers are not burdened by the Ohio investment tax credit as were "purchasers of gas moving through Louisiana in interstate commerce."[160]

Thus, because Ohio's investment tax credit can be distinguished from each of the major cases relied on by the Sixth Circuit, the Supreme Court should conclude, as it has granted certiorari to the *Cuno* appellants' case, that a tax credit based on similar criteria as Ohio's does not discriminate against interstate commerce. Because Ohio's investment tax credit does not discriminatorily tax the products manufactured in another state or the business operations performed in any other state,[161] the Court should conclude that a state's investment tax credit which looks only to in-state operations is a permissible way for the state to structure its tax system to encourage the growth and development of intrastate commerce and industry.[162]

In the meantime, states in the Sixth Circuit—Kentucky, Michigan, Ohio, and Tennessee—are at a distinct disadvantage to states outside the Sixth Circuit which are not bound by the *Cuno* decision.[163] The *Toledo Business Journal* wrote:

> A number of major investment projects in northwest Ohio have been put either on hold or are being reexamined as a result of the Sixth Circuit US Court of Appeals' decision in *Cuno v. DaimlerChrysler* on September

160. *Id.* at 760.

161. *See* Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336-37 (1977).

162. *See id.* at 336.

163. *See generally* Petition for Rehearing with Suggestion for Rehearing En Banc of Appellee, Cuno v. DaimlerChrysler, Inc., 386 F.3d. 738 (6th Cir. 2004) (No. 01-3960). The appellee noted that:

> [I]f the panel's reasoning is correct, hundreds of state statutes are at risk, the financial operations of thousands of businesses will be disrupted, and the economic planning of states and localities across the land will be thrown into disarray. Yet if other courts recognize the errors in the panel's reasoning, every state outside [the Sixth] Circuit will be free to compete for jobs and economic development with a powerful tool that the panel has taken away from Ohio, Kentucky, Michigan, and Tennessee.

Id. at 8; *see also* Brief of Amicus Curiae Mich. Econ. Dev. Corp. at 7-10, Cuno v. DaimlerChrysler, Inc., 386 F.3d. 738 (6th Cir. 2004) (No. 01-3960) (noting the "chilling" effect the court's decision is likely to have on economic development within Michigan and the negative impact on Michigan's ability to compete not only with other states but also internationally); Brief of Amici Curiae Michigan et al. at 6-7, Cuno v. DaimlerChrysler, Inc., 386 F.3d. 738 (6th Cir. 2004) (No. 01-3960) (noting the court's decision will undoubtedly have a chilling effect on capital development projects in all industries in Michigan, Kentucky, and Tennessee).

> 2[,] [2004]. These projects represent the retention of hundreds of existing area jobs and the opportunity to add hundreds of new high paying positions for residents of northwest Ohio. . . . In September, the Regional Growth Partnership was close to announcing a major project in the area. . . . [T]his project and its new jobs have been put on hold by the client as a result of the Sixth Circuit's ruling. The client is now looking at putting this project in Indiana, which is not affected by the Sixth Circuit's ruling.[164]

B. Even Within the Sixth Circuit, All Is Not Dead

Yet, even within the Sixth Circuit, not all economic development tax incentive measures are dead. The Sixth Circuit held that the Ohio personal property tax exemption did not violate the dormant Commerce Clause.[165] The court noted that the statute,[166] which requires an investment in new or existing property within an enterprise zone and the maintenance of employees, "does not impose specific monetary requirements, require the creation of new jobs, or encourage a beneficiary to engage in an additional form of commerce independent of newly acquired property."[167] The court identified the conditions noted as "minor collateral requirements . . . directly linked to the use of the exempted personal property."[168]

The reasoning for maintaining the constitutionality of Ohio's property tax exemption, however, seems to also support maintaining Ohio's investment tax credit. The court stated that "[a]lthough conditions imposed on property tax exemptions may independently violate the Commerce Clause, *conditional exemptions raise no constitutional issues when the conditions for obtaining the favorable tax treatment are related to the use or location of the property itself*."[169] Ohio's investment tax credit was conditioned on the property being installed in Ohio. This was the plaintiffs' central argument and a consideration by the court in striking down the investment tax credit as discriminating against interstate commerce.[170]

However, the court went on to provide that "an exemption may be discriminatory if it requires the beneficiary to engage in another form of business in order to receive the benefit or *is limited to businesses with a specified*

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164. *Court Ruling Jeopardizes Ohio Projects*, *supra* note 5, at 1.

165. *Cuno*, 386 F.3d at 748.

166. OHIO REV. CODE ANN. § 5709.62(C)(1) (West 2004) (permitting municipalities to offer specified incentives to an enterprise that "agrees to establish, expand, renovate, or occupy a facility and hire new employees, or preserve employment opportunities for existing employees" in economically depressed areas).

167. *Cuno*, 386 F.3d at 747.

168. *Id.*

169. *Id.* at 746 (emphasis added).

170. *Id.* at 743.

economic presence."[171] Ohio's investment tax credit was limited to businesses with a "specified economic presence." Specifically, the court noted that section 5733.33(C)(1) provided: "The investment tax credit is generally 7.5 percent 'of the excess of the cost of the new manufacturing machinery and equipment purchased during the calendar year for use in a county over the county average new manufacturing machinery and equipment investment for that county.'"[172] Even so, the court concluded that "if the conditions imposed on the exemption do not discriminate based on an independent form of commerce, they are permissible."[173]

In its explanation, the court noted that there are fundamental differences between credits and exemptions: an investment tax credit reduces preexisting income tax liability, whereas a personal property exemption does not reduce any existing property tax liability.[174] Thus, as the court explained:

> [A] taxpayer's failure to locate new investments within Ohio simply means that the taxpayer is not subject to the state's property tax at all, and any discriminatory treatment between a company that invests in Ohio and one that invests out-of-state cannot be attributed to the Ohio tax regime or its failure to reduce current property taxes.[175]

The court also noted that "the personal property tax exemption is internally consistent because, if universally applied, the new property would escape tax liability irrespective of location. Every new investment, no matter where undertaken, would be exempt from a tax."[176] Would this not also be the case if every state provided an investment tax credit?

The court did not provide direct authority for its assertions in upholding Ohio's property tax exemption, but it did compare *Maryland v. Louisiana* as an example of an unconstitutional tax benefit.[177] The court did, however, refer to a law review article authored by Professors Hellerstein and Coenen who concluded that property tax incentives that offer an exemption or abatement for new investment in the state, without collateral requirements discrete from the use or location of the property itself, should survive constitutional scrutiny.[178] Professors Hellerstein and Coenen distinguished property tax exemptions from investment tax credits by providing first, that credits favor in-state activity by invariably confining the credit in-state and second, they implicate the coercive power of the state by allowing taxpayers to reduce their state tax only by

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171. *Id.* at 746 (emphasis added).

172. *Id.* at 741 (quoting OHIO REV. CODE ANN. § 5733.33(C)(1) (West 2004)).

173. *Cuno*, 386 F.3d at 747.

174. *Id.*

175. *Id.*

176. *Id.* at 748.

177. *Id.* at 746.

178. *Id.* at 747-48; *see also* Hellerstein & Coenen, *supra* note 126, at 825-29 (concluding that property tax exemptions for the most part survive constitutional scrutiny under their "in-state/state-coercion" approach).

engaging in in-state activity.[179] The distinguishing factors between the two, for Professors Hellerstein and Coenen, are that "[property tax incentives] do not favor in-state over out-of-state investment, if one assumes—as one ought to—that other states have adopted taxing regimes similar to the one in question."[180] Neither do property tax incentives implicate the "coercive power of the state" since a taxpayer does not reduce an otherwise existing in-state property tax liability by acquiring property in the state.[181]

Consequently, states within the Sixth Circuit, though not completely stripped of all tax incentives which can be offered, are much more limited than those states outside the Sixth Circuit. How will other income tax incentives fare based on the broad interpretation by the Sixth Circuit of tax incentives that burden interstate commerce?

IV. STATE TAX INCENTIVES—HERE TODAY . . . GONE TOMORROW?

Today every state provides tax incentives to induce industrial location and expansion.[182] "Indeed, scarcely a day goes by without some state offering yet another tax incentive to spur economic development, often in an effort to attract a particular enterprise to the state."[183] Yet, in light of the Sixth Circuit's decision in *Cuno*, how will these tax incentives fare under constitutional scrutiny? If the Supreme Court were to follow the holding of the Sixth Circuit Court of Appeals, virtually no state income tax credit, the most common form of state tax incentive in the country,[184] could meet the appeals court's broad requirement of strict geographic neutrality. Any investment tax credit, similar to Ohio's, that is based on in-state investment;[185] or any research and development credit based on in-state research activity;[186] or credits to business enterprises that increase in-state

179. Hellerstein & Coenen, *supra* note 126, at 817.

180. *Id.* at 825.

181. *Id.*

182. Hellerstein, *supra* note 4, at 413.

183. *Id.*

184. Hellerstein & Coenen, *supra* note 126, at 817.

185. *See, e.g.*, CAL. REV. & TAX. CODE § 23649 (West 2005) (providing a credit equal to six percent of qualified property placed in service "in this state"); COLO. REV. STAT. § 39-22-507.6 (2004) (providing a credit for property "used" in-state); MASS. GEN. LAWS ch. 63, § 31A (2005) (providing investment tax credit for qualified property used in-state); N.J. STAT. ANN. § 54:10A-5.5, 5.6 (West 2004) (providing a credit for in-state investment in new or expanded facility); N.M. STAT. ANN. § 7-9A-5 (LexisNexis 2004) (providing an investment tax credit may be claimed by a qualifying taxpayer carrying on a manufacturing operation in-state); N.C. GEN STAT. § 105-129.9 (2004) (providing a credit for investing in machinery and equipment in-state).

186. *See, e.g.*, ARIZ. REV. STAT. ANN. § 43-1168 (2004) (providing tax credit for increased research activities in-state); N.J. STAT. ANN. § 54:10A-5.24 (West 2004) (providing tax credit for qualified research expenses for research conducted in-state); N.C. GEN. STAT. § 105-129.10 (2004) (providing a tax credit for in-state apportioned research expenses).

employment[187] would fail constitutional scrutiny.

A. Professors Hellerstein and Coenen vs. Professor Enrich

Professors Hellerstein and Coenen would agree with that result based on their in-state favoritism/state-coercion rationale. Under their test, state income tax credits fail to pass muster first, because they favor in-state over out-of-state activity since income tax credits are almost invariably confined to the former, and second, because they implicate the coercive power of the state since the taxpayer can reduce its state tax bill only by engaging in in-state activity.[188] In addition to invalidating income tax credits, their in-state favoritism/state-coercion rationale of analyzing state tax incentives would invalidate many, if not most, tax incentives.[189] Professors Hellerstein and Coenen characterized the state, in effect, as saying:

> You 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.[190]

Still, under the Hellerstein and Coenen approach, there is at least one category of tax incentives that should escape invalidation: tax incentives which are not exemptions from or reductions of an existing state tax liability but rather are exemptions from or reductions of an additional state tax liability to which the taxpayer would be subjected only if the taxpayer were to engage in the targeted activity in the state.[191] Results under this test, at least in some instances, would depend on whether the taxpayer had previously engaged in some taxable activity within the state.[192] In contrast to income tax incentives, Hellerstein and Coenen characterized the state's posture related to property tax exemptions as: "Come to our state and we will not saddle you with any additional property tax burdens. Moreover, should you choose not to accept our invitation, nothing will happen to your tax bill—at least nothing that depends on our taxing regime."[193] Therefore, based on their test, even though income tax credits would be invalid, property tax abatements based on new in-state investments or sales and use tax exemptions for the construction of new facilities in the state (unless tied to other

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187. *See, e.g.*, GA. CODE ANN. § 48-7-40 (2004) (providing a tax credit based on additional new jobs created in-state); *id.* § 48-7-40.5 (providing a tax credit for retraining of resident employees); N.C. GEN STAT. § 105-129.8 (2004) (providing a tax credit for creating new full-time jobs in-state); S.C. CODE ANN. § 12-6-3360 (2004) (providing a jobs tax credit to qualified employers based on location of job creation in-state).

188. Hellerstein & Coenen, *supra* note 126, at 817.

189. *Id.* at 806-07.

190. *Id.* at 808.

191. *Id.* at 807.

192. Schaefer, *supra* note 1, at 325.

193. Hellerstein & Coenen, *supra* note 126, at 808.

in-state activity such as job creation or a certain size of enterprise) would be "valid since the state is merely 'disclaiming the right to impose any taxes on a 'virgin' tax base the state is seeking to attract.'"[194]

Professor Enrich advocates that when analyzing the constitutionality of state location incentives for businesses, it is the antidiscrimination principle that is of primary significance.[195] Indeed, "the prohibition against state tax provisions that discriminate against interstate commerce has been a central tenet of the Court's Commerce Clause case law throughout its history. . . ."[196] Professor Enrich suggests, however, that instead of the in-state favoritism/state-coercion test advocated by Professors Hellerstein and Coenen, "the primary focus in determining whether a particular tax provision runs afoul of the antidiscrimination principle is a practically oriented analysis of the provision's purposes and effects."[197] Under the anti-discrimination principle, with the focus being on discrimination against out-of-state businesses or interests, "a property tax or sales tax abatement is unlikely to be struck down for out-of-state businesses are not responsible for these taxes and thus there can be no discrimination against these businesses."[198] In contrast, a state investment tax credit given only for in-state investment would likely be struck down since it discriminates against out-of-state business activity by requiring the business to conduct its business in-state in order to receive the credit.[199]

Professor Enrich argues, though, that Commerce Clause values are broader than merely discrimination against out-of-state interests.[200] He argues that the primary objective of the Commerce Clause is to create and preserve an open interstate economy, "a national common market."[201] He is concerned with distortions caused to the national economy, economic balkanization, and rivalries between the states.[202] He maintains that the focus in evaluating a tax incentive "should be 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."[203] Under this more restrictive approach (as compared to the Hellerstein/Coenen test), the property tax abatement would be treated the same as an investment tax credit: both would be illegal.[204]

Professor Enrich offers that the Court has the opportunity to strengthen and clarify its Commerce Clause jurisprudence by reframing the antidiscrimination

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194. Schaefer, *supra* note 1, at 325 (quoting Hellerstein & Coenen, *supra* note 126, at 809).

195. Enrich, *supra* note 2, at 426.

196. *Id.*

197. *Id.* at 432.

198. Schaefer, *supra* note 1, at 325.

199. *Id.*

200. Enrich, *supra* note 2, at 453.

201. *Id.* at 454 (quoting Hunt v. Wash. State Apple Adver. Comm'n, 432 U.S. 333, 350 (1977)).

202. *Id.* at 454-55.

203. *Id.* at 456.

204. Schaefer, *supra* note 1, at 326.

principle, specifically, by "prohibit[ing] state tax measures that discriminate against interstate commerce by distorting the decisions of economic actors in favor of expenditures on in-state activities."[205] Under this reframed antidiscrimination principle, economic development "location incentives would be virtually per se unconstitutional."[206] These incentives "would be condemned, not because they commonly have the effect of placing out-of-state activities at a relative disadvantage, nor because they typically distinguish on their face between in-state and out-of-state activity, but because their central function is to influence economic location decisions and to divert investment into the state."[207]

The Sixth Circuit, by upholding Ohio's property tax exemption in *Cuno*, clearly rejected Professor Enrich's more restrictive approach of analyzing location tax incentives.[208] Instead, the holding followed the logic of Hellerstein and Coenen's in-state favoritism/state-coercion rationale.[209] Even this rationale, though, is much too broad based on Supreme Court Commerce Clause precedent. It seems, that based on the Court's own reasoning, the test should be who bears the burden? In other words, who pays the price to "lure" the new business, or expansion of an existing business, in-state? Is this cost borne generally by citizens in-state who have their own competing demands, or is the cost borne by firms out-of-state that have chosen a lesser economic presence?

B. One More Look at Subsidies

The defendants in *Cuno*, alternatively, likened the Ohio investment tax credit to a direct subsidy. The Sixth Circuit, however, quickly dismissed that argument citing *New Energy Co. of Indiana* and *West Lynn Creamery*.[210] The appeals court noted that the distinction, in the constitutional sense, between a subsidy and a tax credit results from the fact that the tax credit involves state regulation of interstate commerce through its power to tax.[211] The Court, however, has acknowledged in *Camps Newfound/Owatonna, Inc. v. Town of Harrison*[212] that "tax exemptions and subsidies serve similar ends."[213]

Even so, holdings of the Court have rested on the premise that "there is a constitutionally significant difference between subsidies and tax exemptions."[214]

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205. Enrich, *supra* note 2, at 457-58.

206. *Id.* at 458.

207. *Id.*

208. *See* Cuno v. DaimlerChrysler, Inc., 386 F.3d 738, 748 (6th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3751 (U.S. Sept. 27, 2005) (No. 04-1704); *see also id.* at 740 (noting that Professor Enrich served as counsel for plaintiffs in *Cuno*).

209. *Id.* at 747.

210. *Id.* at 746.

211. *Id.*

212. 520 U.S. 564 (1997).

213. *Id.* at 589.

214. *Id.* at 590; *see also* Walz v. Tax Comm'n of New York, 397 U.S. 664, 673 (1970) (holding that New York's tax exemption for church property did not violate the Establishment

The taxpayer in *Camps Newfound/Owatonna* was a nonprofit corporation in Maine that operated a summer camp for the benefit of children of the Christian Science faith.[215] Because the camp predominately served nonresidents, the relevant Maine statute[216] denied the camp an exemption from local real estate taxes, even though an otherwise identical camp serving in-state residents would be exempt from local real estate taxes.[217] The Court concluded that it was not necessary to look beyond the text of the statue to determine that it discriminated against interstate commerce.[218] Even though the statute was determined to be *per se* discriminatory, the Town argued, among other things, that the statute should be viewed as a legitimate discriminatory subsidy to those charities that choose to focus their activities on local concerns. Since a direct subsidy would pass constitutional muster,[219] the Town argued that exemption statute should satisfy Commerce Clause requirements as well.[220] The Court disagreed, though Professor Zelinsky commented, "in a fashion that is not wholly convincing."[221] The *Camps Newfound/Owatonna* decision is significant, not only because the Court reiterated that it has not squarely confronted the constitutionality of subsidies, but also because the majority along with the dissenters "underscored the untenability" of the tax/subsidy distinction.[222]

The majority cited *Walz* for the proposition "that there is a constitutionally significant difference between subsidies and tax exemptions"[223] However, just prior to its invocation of *Walz*, the *Camps Newfound/Owatonna* Court noted, "somewhat confusingly,"[224] that "[w]e recognized long ago that a tax exemption can be viewed as a form of government spending."[225] "At best, this observation required an explanation as to when conventional expenditures are (and are not)

Clause of the First Amendment, relying, in part, on the premise that there is a constitutionally significant difference between subsidies and tax exemptions).

215. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 567.

216. ME. REV. STAT. ANN., tit. 36, § 652(1)(A) (1996).

217. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 569; *see* Edward A. Zelinsky, *Are Tax "Benefits" Constitutionally Equivalent to Direct Expenditures?*, 112 HARV. L. REV. 379, 387 (1998) [hereinafter Zelinsky, *Tax Benefits*].

218. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 575-76.

219. Even though the Town argued that a direct subsidy is constitutional, the Court did not reach the question whether the hypothesized subsidy would survive constitutional challenge. Instead, it explicitly noted that the issue of subsidies was not before it and need not be addressed today. Indeed, the Court merely "[a]ssum[ed], *arguendo*, that the Town [was] correct that a direct subsidy benefiting only those nonprofits serving principally Maine residents would be permissible . . . ." *Id.* at 589.

220. *Id.* at 588-89.

221. Zelinsky, *Tax Benefits*, *supra* note 217, at 387.

222. Zelinsky, *Restoring Politics to the Commerce Clause*, *supra* note 135, at 43.

223. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 590; *see* Zelinsky, *Tax Benefits*, *supra* note 217, at 387.

224. Zelinsky, *Tax Benefits*, *supra* note 217, at 387.

225. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 589 n.22.

equivalent to tax benefits—an explanation that the Court did not provide; at worst, this observation contradicted the Court's simultaneous, *Walz*-based assertion that tax benefits and direct spending are different."[226] Furthermore, the Court never articulated its rationale for rejecting the Town's claim.[227] It did, however, reiterate its oft-quoted statement from *West Lynn Creamery* that "[w]e have 'never squarely confronted the constitutionality of subsidies,' and we need not address these questions today."[228]

The *Camps Newfound/Owatonna* decision is significant for another reason: the dissenting justices underscored the problems of the Court's dormant Commerce Clause case law.[229] Justice Scalia, also writing for Chief Justice Rehnquist and Justices Thomas and Ginsburg, began by noting:

> The Court's negative Commerce Clause jurisprudence has drifted far from its moorings. . . . Our cases have struggled (to put it nicely) to develop a set of rules by which we may preserve a national market without needlessly intruding upon the States' police powers, each exercise of which no doubt has some effect on the commerce of the Nation.[230]

Even though Justice Scalia declared, just as he had done in *New Energy Co. of Indiana*, that "direct subsidies to domestic industry do not run afoul of the Commerce Clause[,]"[231] he equated state social services provided only to residents to tax exemptions limited to in-state charities.[232] In Justice Scalia's view:

> [T]he provision by a State of free public schooling, public assistance, and other forms of social welfare to only (or principally) its own residents—whether it be accomplished *directly or by providing tax exemptions, cash, or other property* to private organizations that perform the work for the State—implicates none of the concerns underlying our negative Commerce Clause jurisprudence.[233]

Justice Thomas, writing for himself and Justice Scalia, declared that Maine's tax exemption for certain charities was "in truth, no different than a subsidy paid out of the State's general revenues."[234] He explained that he wrote separately

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226. Zelinsky, *Tax Benefits*, *supra* note 217, at 387.

227. *Id.* at 388.

228. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 589 (quoting West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 199 n.15 (1994)).

229. Zelinsky, *Restoring Politics to the Commerce Clause*, *supra* note 135, at 43.

230. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 595-96 (Scalia, J., dissenting).

231. *Id.* at 597; *see also* New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 278 (1988) (noting direct subsidization of domestic industry does not ordinarily run afoul of the negative Commerce Clause).

232. *Camps Newfound/Owatonna, Inc.*, 520 U.S. at 605-06 (Scalia, J., dissenting).

233. *Id.* at 607-08 (emphasis added).

234. *Id.* at 640 (Thomas, J., dissenting).

because he believed that the Court's expansion of the negative Commerce Clause in *Camps Newfound/Owatonna* was possible only because the Court's "negative Commerce Clause jurisprudence . . . was already both overbroad and unnecessary. . . . That the expansion effected by today's decision finds some support in the morass of our negative Commerce Clause case law only serves to highlight the need to abandon that failed jurisprudence . . . ."[235]

Significantly, not only were Justice Scalia and Justice Thomas asserting the similarities between a tax exemption and a subsidy, they were also advocating abandoning the dormant Commerce Clause jurisprudence altogether. Professor Zelinsky notes that the Justices' desire to abandon the dormant Commerce Clause may explain why they cling to the tax/subsidy distinction despite its logical flaws: if they cannot convince their colleagues to abandon the dormant Commerce Clause, then it tactically makes sense to cabin that Clause as much as possible.[236]

West Lynn Creamery, Inc. v. Healy[237] has been the most recent subsidy case heard by the Court. It involved a Massachusetts pricing order that imposed an assessment on the sale of all fluid milk by dealers to Massachusetts retailers. These payments were placed into a fund that was distributed solely to Massachusetts dairy farmers; however, two-thirds of the milk was produced out-of-state. Even though the subsidy was struck down, it was invalidated "on very narrow grounds."[238] The Court noted that a pure subsidy funded from general revenues ordinarily imposes no burden on interstate commerce, but merely assists local business.[239] The Massachusetts pricing order, however, was funded principally from taxes on the sale of milk produced in other states.[240] The Court explained that by funding the subsidy in that manner, the state "not only assist[ed] local farmers, but burden[ed] interstate commerce. The pricing order thus violate[d] the cardinal principle that a State may not 'benefit in-state economic interests by burdening out-of-state competitors.'"[241]

Even though Justice Scalia, joined by Justice Thomas, concurred in the judgment, he rejected a distinction between subsidies and tax exemptions, concluding that subsidies, whether in the "form of cash" or "tax forgiveness" ultimately "come[] to the same thing."[242] Chief Justice Rehnquist, as did Justice Scalia, rejected the majority's argument that by coupling the tax with the subsidy, those who would have otherwise lobbied against the tax were instead "mollified by the subsidy."[243] The Chief Justice dissented, arguing that the tax and the

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235. *Id.* at 610.

236. Zelinsky, *Restoring Politics to the Commerce Clause*, *supra* note 135, at 46.

237. 512 U.S. 186 (1994).

238. Petrov, *supra* note 20, at 99; *see also West Lynn Creamery, Inc.*, 512 U.S. at 199.

239. *West Lynn Creamery, Inc.*, 512 U.S. at 199.

240. *Id.*

241. *Id.* (quoting New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 273-74 (1988)).

242. *Id.* at 208-09 (Scalia, J., concurring).

243. *Id.* at 214 (Rehnquist, C.J., dissenting); *see id.* at 212 (Scalia, J., concurring) (stating: "as THE CHIEF JUSTICE explains, '[a]nalysis of interest group participation in the political process

subsidy should have been evaluated independently.[244]

These two cases alone show the division of the Court related to the distinction between tax exemptions and subsidies. What is surprising, though, after analyzing the two cases is the conclusion reached by Justice Scalia in *New Energy Co. of Indiana*. *New Energy Co.* exemplifies the inequity of finding a distinction between exemptions and subsidies, of looking at "formal language" rather than the "economic realities."[245] *New Energy Co.* involved an Ohio tax credit designed to encourage the in-state production of ethanol. Ohio allowed a tax credit against the state's motor fuel tax for each gallon of ethanol sold by fuel dealers, but only if the ethanol was produced in Ohio or in a state that granted similar tax advantages to ethanol produced in Ohio.[246] The appellant was an Indiana manufacturer of ethanol. Indiana had repealed its tax exemption for ethanol and in its stead passed legislation providing a direct subsidy to Indiana ethanol producers. Thus, by reason of Ohio's reciprocity provision, appellant's ethanol sold in Ohio was ineligible for Ohio's tax credit.[247] Invoking the nondiscrimination principle, the Court concluded that the provision "explicitly deprive[d] certain products of generally available beneficial tax treatment because they [were] made in certain other States, and thus on its face appear[ed] to violate the cardinal requirement of nondiscrimination."[248]

Justice Scalia, writing for a unanimous Court, interestingly did find in *New Energy Co.* a distinction between a tax exemption and a subsidy, nonetheless noting that the subsidy was no less discriminatory than the tax credit being attacked.[249] Between 1988 when, *New Energy Co.* was decided, 1994, when *West Lynn Creamery* was decided, and 1997, when *Camps Newfound/Owatonna* was

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may serve many useful purposes, but serving as a basis for interpreting the dormant Commerce Clause is not one of them'").

244. *Id.* at 214-16 (Rehnquist, C.J., dissenting).

245. *See* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977) (noting for Commerce Clause purposes, it is "not the formal language of the tax statute but rather its practical effect" that should control).

246. *See* OHIO REV. CODE ANN. § 5735.145(B) (West 1986).

247. New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 272-73 (1988).

248. *Id.* at 274.

249. *Id.* at 278. Noting the distinction, the Court provided:

> It has not escaped our notice that the appellant here, which is eligible to receive a cash subsidy under Indiana's program for in-state ethanol producers, is the potential beneficiary of a scheme no less discriminatory than the one that it attacks, and no less effective in conferring a commercial advantage over out-of-state competitors. To believe the Indiana scheme is valid, however, is not to believe that the Ohio scheme must be valid as well. The Commerce Clause does not prohibit all state action designed to give its residents an advantage in the marketplace, but only action of that description *in connection with the States regulation of interstate commerce*. Direct subsidization of domestic industry does not ordinarily run afoul of that prohibition; discriminatory taxation of out-of-state manufacturers does.

Id. (emphasis added).

decided, the Court became divided on the issue of whether or not there is a distinction between tax exemptions and subsidies. Even with this division, it seems the Court would find a subsidy funded from the state's general treasury constitutional and would find unconstitutional a specific tax imposed predominately on out-of-state tax taxpayers. At this juncture, however, the Court majority has not equated a tax exemption and a direct subsidy. Thus, notwithstanding the lack of explanation, the Sixth Circuit, in dismissing the argument of the *Cuno* plaintiffs that Ohio's investment tax credit was like a direct subsidy, did follow Supreme Court precedent.

Nonetheless, based on the reasoning of *West Lynn Creamery*, it follows that states that fund tax exemptions and credits from an economic development fund which is funded by the general assembly should pass constitutional scrutiny.[250] Assuming, as the Court did in *West Lynn Creamery*, that both Massachusetts's exemption and subsidy standing alone would have been constitutional, the pricing order was nevertheless struck down because the subsidy was funded principally from taxes on the sale of milk produced out-of-state rather than from the state's general revenue.[251] For the states that have created economic development funds, in-state interests can lobby against the appropriations for economic development if they so desire.[252] In this manner, the state's political processes can be relied upon "to prevent legislative abuse."[253]

CONCLUSION

The Sixth Circuit has placed a very heavy burden on the states within its jurisdiction. Those states—Kentucky, Michigan, Ohio, and Tennessee—are no longer on the same economic development playing field with the rest of the nation. When the Supreme Court addresses the issue of economic development tax incentives in its review of *Cuno v. DaimlerChrysler*, it need not even get to the issue of whether the tax incentive is similar to a subsidy. The Court should look to who is bearing the burden. In other words, who pays the price to "lure" the new business, or expansion of an existing business, in-state? Is this cost borne generally by citizens in-state who have their own competing demands, or is the cost borne by out-of-state competitors? The analysis of Justice Brickley in *Caterpillar, Inc.* provides a guide: "Basing a deduction on a change in a

250. *See* COLO. REV. STAT. ANN. § 24-46-105 (West 2004) (creating Colorado economic development fund subject to annual appropriation by the general assembly); 35 ILL. COMP. STAT. 10/5-85 (2004) (funding tax credit awarded to taxpayer meeting economic development criteria from "Economic Development for a Growing Economy Fund" which is funded in part from appropriations from the general assembly); IND. CODE § 6-3.1-13-26 (2004) (funding tax credit awarded to taxpayer meeting economic development criteria from "economic development for a growing economy fund" which is funded in part from appropriations from the general assembly); *cf.* 12 PA. CONS. STAT. ANN. § 3706(c) (West 2004) (providing limitation of $25 million for approved tax credits).

251. West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 199 (1994).

252. *See id.* at 200.

253. *Id.*

subset of a company's in-state activity relative to its total activity is unconstitutional."[254] In that situation, just as in *Westinghouse Electric Corp.*, out-of-state competitors do bear the burden of "economic protectionism." However, where the incentive is available equally to in-state and out-of-state businesses, without reference to a subset of the company's activities, the incentive should pass constitutional scrutiny. Likewise, states that fund their economic development tax credits and exemptions from general revenue appropriations should also pass constitutional scrutiny.

Nevertheless, the holding by the Sixth Circuit invalidating Ohio's investment tax credit misapplied previous Supreme Court precedent. It failed to recognize crucial distinctions. As a result, the broad holding of the Sixth Circuit would invalidate virtually every income tax credit or deduction provided as an economic development incentive. A decision of a business to expand in-state or to locate within a state necessarily is a benefit to one state and a detriment to all others.[255] Yet, that should not be the basis to nullify incentives provided throughout this country. States, businesses, communities, and individuals have relied on development incentives and have planned accordingly.[256]

Arguably, "competition among the states in the form of development incentives was a concern for the drafters of the Constitution in vesting the federal government with the commerce power."[257] Writing on commercial competition as a source of contention among the states in *The Federalist*, Alexander Hamilton "expressed particular worry about states adopting commercial policies peculiar to themselves, creating 'distinctions, preferences, and exclusions, which would beget discontent.'"[258] Yet, Alexander Hamilton, even with his concerns regarding commercial competition, was granted a tax abatement in 1791 by the state of New Jersey to start a business.[259]

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254. Caterpillar, Inc. v. Dep't of Treasury, 488 N.W.2d 182, 216 (Mich. 1992) (Brickley, J., dissenting in part).

255. *See* The State of Ohio's Petition for Rehearing, Cuno v. DaimlerChrysler, Inc., 386 F.3d 738 (6th Cir. 2004) (No. 01-3960) (noting that *any* growth in one state comes at the expense of development in other states).

256. Brief of Amici Curiae Louisville Area Chamber of Commerce, Inc. et al. at 7, Cuno v. DaimlerChrysler, Inc., 386 F.3d 738 (6th Cir. 2004) (No. 01-3960) (citing Quill Corp. v. North Dakota, 504 U.S. 298, 317 (1992), which "declin[ed] to reverse a longstanding position on the states' methods of taxing mail order businesses because existing precedents had 'engendered substantial reliance and [had] become part of the basic framework of a sizable industry'").

257. Ivan C. Dale, Comment, *Economic Development Incentives, Accountability Legislation and a Double Negative Commerce Clause*, 46 ST. LOUIS U. L.J. 247, 272 (2002).

258. *Id.* (quoting THE FEDERALIST No. 7, at 29 (Alexander Hamilton) (Bantam Classic ed., 1982)).

259. *Id.*