No.

In the Supreme Court of the United States

DAIMLERCHRYSLER CORPORATION,

Petitioner,

v.

CHARLOTTE CUNO, ET AL.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether Ohio's investment tax credit, Ohio Revised Code § 5733.33, which seeks to encourage economic development by providing a credit to taxpayers who install new manufacturing machinery and equipment in the State, violates the Commerce Clause of the United States Constitution.

RULE 29.6 STATEMENT AND PARTIES TO THE PROCEEDING

Pursuant to this Court's Rule 29.6, petitioner states that DaimlerChrysler Corporation is a wholly owned subsidiary of DaimlerChrysler North America Holding Corporation, which in turn is a wholly owned subsidiary of DaimlerChrysler A.G.

The parties to the proceeding in the court of appeals were plaintiffs Charlotte I. Cuno, Duane M. Arquette, Robert Scott Brundage, Julie Coyle, Helen Czapczynski, Mary Ebright, Carrie Hawkins, Kathleen Hawkins, Hutton Pharmacy, Inc., Jean E. Kaczmarek, Kim's Auto and Truck Servive, Inc., Judith A. Pfaff, Kenneth P. Pfaff, Phoenix Earth Food Co-op, Inc., Carol A. Raschke, Herbert H. Raschke, Rick Van Landingham, and defendants DaimlerChrysler Corporation, the Toledo Public School District, the Washington Local School District, the City of Toledo, the State of Ohio, the Ohio State Treasurer, the Ohio Department of Taxation, and the Ohio Department of Development.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner DaimlerChrysler Corporation ("DaimlerChrysler") respectfully petitions the Court to grant a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-17a) is reported at 386 F.3d 738. The order of the court of appeals denying rehearing (App., *infra*, 31a) is unreported. The opinion of the district court (App., *infra*, 18a-30a) is reported at 154 F. Supp. 2d 1196.

JURISDICTION

The court of appeals' judgment was entered on October 19, 2004. A timely petition for rehearing was denied on January 18, 2005. On April 7, 2005, Justice Stevens extended the time for filing a petition for a writ of certiorari to and including June 17, 2005. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause of the United States Constitution, Art. I, § 8, cl. 3, provides in relevant part:

> The Congress Shall have the Power * * * To Regulate commerce * * * among the several States.

Ohio Revised Code § 5733.33 is reproduced in the appendix to this petition at 32a-43a.

STATEMENT

In this case, the Sixth Circuit held that the State of Ohio violates the Commerce Clause by offering business income tax incentives to encourage economic development in the

State. This holding is one of enormous practical and doctrinal importance: it calls into question the constitutionality of hundreds of similar tax programs offered by a substantial majority of the states. The uncertainty caused by the Sixth Circuit's decision accordingly has thrown into disarray the job creation efforts and economic planning of states and localities across the Nation, while disrupting the investment decisions of thousands of businesses. Because that holding also cannot be reconciled with a decision of the highest court of a state in the Sixth Circuit, rests on a novel legal theory that departs from principles announced by this Court, and finds no support in the policies of the Commerce Clause, further review is warranted. Given the significance of the issue presented here, it plainly should be this Court, and not the Sixth Circuit, that provides guidance to states and taxpayers across the country on the permissible use of business tax incentives.

1. Ohio's Income Tax Credit

"Today, every state provides tax and other economic incentives as an inducement to local industrial location and expansion." Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 790 (1996) (footnotes omitted). Such "[l]ocation[al] incentives have become an ubiquitous feature of the state tax scene." Peter Enrich, *Saving the States From Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 384 (1996). And of the myriad state and local provisions that are intended to attract and encourage business development, "[t]he most common form of state tax incentive in this country is the income tax credit." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 817.

This case involves a constitutional challenge to such a provision, Ohio's investment tax credit (or "ITC"), which is typical of business development income tax incentives offered by states across the country.[1] Ohio's ITC provides that a taxpayer may receive a "nonrefundable credit * * * against the tax imposed by section 5733.06 of the Revised Code" (Ohio's corporate franchise tax, which is based on corporate income or net worth) if the taxpayer "purchases new manufacturing machinery and equipment" during a qualifying period and installs the equipment in Ohio by December 31, 2006. Ohio Rev. Code ("O.R.C.") § 5733.33(B)(1). This investment tax credit of seven and one-half percent is available in an amount equal to "the cost of the new manufacturing equipment purchased during the calendar year for use in a county" over and above the average annual cost of new manufacturing machinery and equipment purchased by the taxpayer for use in that county during three specified prior years.[2] The credit amount increases to 13½ percent if the otherwise qualifying investment is made in an "eligible area" that suffers from specified levels of unemployment or poverty, or has experienced significant closing or downsizing by

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[1] Ohio law also provides that a municipal corporation may offer a property tax exemption to an enterprise that develops facilities or preserves employment in a distressed area. O.R.C. § 5709.62. Pursuant to this provision, DaimlerChrysler received a ten-year, 100% exemption from taxes on certain personal property first used in connection with its plant in Toledo. See App., *infra*, 2a. Although plaintiffs challenged the constitutionality of the property tax exemption, the district court and the Sixth Circuit both upheld that provision. *Id*. at 11a-14a. Plaintiffs have sought review of that aspect of the decision below in a petition now pending before the Court, No. 04-1407, *Cuno* v. *DaimlerChrysler, Inc.* DaimlerChrysler is responding to that petition in a separate brief.

[2] For credits claimed in 1999 and thereafter, the baseline period is the years six, five, and four years before the year for which the credit is claimed. Thus, for example, to determine whether an investment in 2000 is eligible for any credit, one would compare the amount invested in 2000 with the average amount invested by the taxpayer in that same county in 1994, 1995, and 1996.

local employers. *Id.*, §§ 5733.33(C)(2), (A)(8)-(16). The credit may not exceed $1,000,000 unless, in the year for which it is claimed, the taxpayer has increased its overall ownership of manufacturing equipment in the State. *Id.*, § 5733.33(B)(2)(a).

The ITC has been a significant tool used by Ohio to encourage in-state investment. In its petition seeking rehearing before the Sixth Circuit, Ohio represented that, since the credit's inception in 1995, corporations have relied upon the provision in investing more than $30 billion in Ohio plants and equipment. No. 01-3960, *Cuno* v. *DaimlerChrysler Corp.* (6th Cir.), Ohio's Pet. For Reh'g, at 4. In 2002 alone, more than 2,100 corporate taxpayers took Ohio ITC credits totaling more than $73 million. *Ibid*.

2. Background Of The Litigation

On November 12, 1998, petitioner DaimlerChrysler entered into an agreement with the City of Toledo, Ohio, to construct a new vehicle assembly plant near the company's existing facility in the City. App., *infra*, 2a. DaimlerChrysler estimated that it would invest approximately $1.2 billion in the new plant and that, as a result of the investment, the project would provide jobs for thousands of workers. *Ibid*. As an incentive for DaimlerChrysler to undertake the project, which is located within an economically distressed area, the City and the affected local school districts agreed that the company would obtain the tax exemptions that are available under state law. Pursuant to O.R.C. § 5733.33, DaimlerChrysler accordingly has received the investment tax credit of 13½ percent for investments related to the project through December 31, 2000.

Invoking the Constitution's Commerce Clause, the plaintiffs (respondents in this Court), most of whom are local Ohio taxpayers, then brought this action in Ohio state court against DaimlerChrysler, the State of Ohio, and the City of Toledo. Plaintiffs sought to invalidate both the tax credit granted to DaimlerChrysler and the Ohio statute making the credit available. The defendants removed the case to the U.S. District Court for the Northern District of Ohio, which rejected plaintiffs' claims on the merits and ordered the complaint dismissed. App., *infra*, 18a-30a. After canvassing the relevant case law, the court concluded that the "investment tax credit is not akin to a tariff, since it does not burden in the slightest the transfer of goods in interstate commerce," and that the credit also does not punish activity carried on outside Ohio. *Id*. at 28a. The court accordingly held that the tax credit does "not 'discriminate against interstate commerce,'" concluding that it could not find the credit unconstitutional without "violating the clear mandate of Supreme Court precedent." *Id*. at 29a.[3]

3. The Decision Below

The Sixth Circuit reversed in relevant part, holding the investment tax credit unconstitutional. App, *infra*, 1a-17a. The court began by recognizing that "it is legitimate for Ohio to structure its tax system to encourage new interstate economic activity" and that the Commerce Clause does not "prevent a state from 'compet[ing] with other States for a share of interstate commerce.'" *Id*. at 4a-5a (quoting *Boston Stock Exch.* v. *State Tax Comm'n*, 429 U.S. 318, 336-337 (1977)). The court also acknowledged that "the investment tax credit at issue here is equally available to in-state and out-of-state businesses." *Id*. at 6a. And noting the defendants' argument that "tax incentives, like the Ohio tax credit, are permissible so long as they do not penalize out-of-state economic activity," the court of appeals agreed that "it is arguably possible to fit certain of the Supreme Court's cases into this framework." *Id*. at 9a. The court added that the Supreme

[3] In addition, the district court rejected claims challenging the ITC and the property tax exemption under the equal protection clause of the Ohio Constitution. The court of appeals affirmed that holding. See App., *infra*, 14a-17a.

Court "has never precisely delineated the scope of the doctrine that bars discriminatory taxes." *Id*. at 5a.

Having said all that, however, the court of appeals nevertheless went on to hold that Ohio's investment tax credit violates the Commerce Clause. In doing so, the court appeared to accept plaintiffs' argument that the credit is invalid because its "economic effect * * * is to encourage further investment in-state at the expense of development in other states and that the result is to hinder free trade among the states." App., *infra*, 9a. To reach this conclusion, the court found no meaningful distinction "between laws that benefit in-state activity and laws that burden out-of-state activity" because, "economically speaking, the effect of a tax benefit or burden is the same." *Id.* at 9a, 10a. At the same time, the court rejected defendants' argument that the investment tax credit should be likened to a "direct subsidy," even though a subsidy and the credit "would no doubt have the same economic effect." *Id*. at 10a. Accordingly, although the court declared itself "sympathetic to efforts by the City of Toledo to attract industry into its economically depressed areas" (*id*. at 11a), it reversed "that portion of the district court's judgment upholding as constitutional the investment tax credit provision." *Ibid*.

REASONS FOR GRANTING THE PETITION

The Sixth Circuit's decision in this case involves a question of exceptional importance. Invoking the Commerce Clause, the court of appeals invalidated a crucial tool used by Ohio to retain employment and further economic development. And the decision below has an impact that far transcends Ohio's borders, calling into question the constitutionality of very similar economic development laws that are in force in states across the Nation – thus disrupting ongoing efforts to foster investment and job creation.

That decision should not stand. It is inconsistent with the settled understanding that the Commerce Clause's anti-discrimination principle was designed to invalidate *protectionist* state legislation that provides a competitive advantage to in-state businesses, and has no role to play when – as is true in this case – the sole purpose of a challenged state law is to reward intrastate investment. As this Court has explained repeatedly, nothing in the Constitution prevents a state from "compet[ing] with other States for a share of interstate commerce; such competition lies at the heart of a free trade policy." *Boston Stock Exch.*, 429 U.S. at 336-337. That is precisely what Ohio is doing here. Indeed, the Sixth Circuit's ruling directly conflicts with the Michigan Supreme Court's decision upholding a Michigan tax abatement statute that was designed to encourage local investment in that State. Because the decision below has thrown into confusion both the business incentive programs of dozens of states and fundamental Commerce Clause doctrine, review of that decision by this Court plainly is in order.

A. The Decision Below Involves A Recurring Issue Of Great Practical Importance

1. The Sixth Circuit's Decision Has Disrupted State Income Tax Abatement Programs Nationwide

At the outset, the extraordinary importance of this case to the national economy and to economic development in states across the Nation makes review of the Sixth Circuit's decision imperative. There is no denying that the court of appeals' holding "sent shock waves throughout the state and local tax community" and that, "[g]iven the widespread use of similar legislation[,] the potential ramifications [of the decision] nationwide are staggering." Timothy Gillis, *Sixth Circuit Bans Ohio Tax Credit Under the Dormant Commerce Clause, Casting a Pall on Incentives*, 101 J. TAX'N 359, 359 (2004). As we explain below, the Sixth Circuit's holding is inconsistent with the approach taken by this and other courts. But even if that were not the case, the far-reaching implications of the decision would warrant immediate review by this Court. Indeed, "[i]n light of the importance of the issues raised by this case," plaintiffs have represented that they "do not intend to oppose [the] petitions for review of the constitutionality of Ohio's tax credit." No. 04-1407, *Cuno* v. *DaimlerChrysler, Inc.*, Pet. For Cert., at 7.[4]

As has been widely noted, the rule announced by the Sixth Circuit has implications for the validity of literally hundreds of statutes in dozens of states. Virtually all states provide tax and similar economic incentives for local economic activity. See, *e.g.*, Chris Micheli, *A 50-State Comparison of Tax Incentives for Manufacturing Equipment Purchases*, 12 STATE TAX NOTES 1739 (1997); 1 MULTISTATE CORPORATE INCOME TAX GUIDE (CCH Internet) ¶ 180 (2001). And income tax benefits of the sort invalidated by the Sixth Circuit are "the most common form of tax incentive." Hellerstein & Conen, *supra*, 81 CORNELL L. REV. at 797. See Enrich, *supra*, 110 HARV. L. REV. at 384.[5] Tax abatement provisions thus "constitute long-standing, familiar, and central features of every state's taxing system." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 805. The importance of this economic development tool to the states is apparent from the frequency with which it is applied: the aggregate amount of business location tax incentives as of 1996 approached $50 billion (see Kenneth P. Thomas, COMPETING

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[4] That petition should be captioned "*Cuno* v. *DaimlerChrysler Corporation.*"

[5] One study found more than 330 statutory income or franchise tax credits and incentives offered by 46 states. See Gillis, *supra*, 101 J. TAX'N at 360 (citing Mark L. Nachbar, *Credits and Incentives: Alabama Through Hawaii*, 1450 T.M. (BNA) (2005)). Another state-by-state survey "found that, of forty-eight states responding, only Wyoming had not enacted at least one location incentive between 1991 and 1993." Enrich, *supra*, 110 HARV. L. REV. at 383-384.

FOR CAPITAL: EUROPE AND NORTH AMERICA IN A GLOBAL ERA 159-160 (2000)), and doubtless is vastly higher today.

Yet the Sixth Circuit's decision calls into question the constitutionality of all state income tax and related business incentives, most of which are unlikely to be distinguishable from Ohio's in any material respect. See Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 802 ("Almost no state income tax incentive – and there are hundreds of them across the country – meets the * * * requirement of strict geographic neutrality."). As a consequence, "virtually every state in the union has some form of tax credit or incentive that may now be under a constitutional cloud. Moreover, businesses across the country, which have relied on these incentives in making in-state investment decisions, have billions of dollars at stake in the resolution of the controversy." Gillis, *supra*, 101 J. TAX'N at 359.

The result is that the Sixth Circuit's decision is having an immediate impact on state and local governments, businesses, and workers in almost every state. "The decision leaves many states (40 or more), and potentially thousands of businesses, under a cloud of uncertainty about the viability of existing tax incentive arrangements involving billions in capital investment." John Biggins, *Investment Tax Credit Incentive Violates Commerce Clause, Says Sixth Circuit*, 14 J. MULTISTATE TAX'N & INCENTIVES 36, 36 (2004). And this effect is being felt nationwide because the decision below creates doubts about the validity of laws in states *outside* the Sixth Circuit. See Gillis, *supra*, 101 J. TAX'N at 362 ("For taxpayers in other states, both those within and outside the jurisdiction of the Sixth Circuit, the availability of similar incentives is under a pall."). Immediate review by this Court – of a decision that is causing widespread "unpredictability and instability," and thus disrupting economic development efforts across the Nation (Biggins, *supra*, 14 J. MULTISTATE TAX'N & INCENTIVES at 38) – accordingly is warranted.

2. The Decision Below Has Handicapped Economic Development Efforts In The Sixth Circuit

Moreover, review would be in order even if the Court considers only the effects of the decision below on states in the Sixth Circuit. The court of appeals' decision invalidated a statute that is a principal tool used by Ohio and its local governments to maintain employment and encourage economic development. As we have noted, the ITC has been invoked to attract billions of dollars in investment and to retain many thousands of jobs in Ohio over the past decade. Yet the decision below calls an abrupt halt to use of this tool to bolster the State's economy and workforce.

At the same time, the court of appeals' holding places in grave doubt the constitutionality of economic development programs used by all of the other states in the Sixth Circuit.[6] Those laws are now under a cloud – which means that, if states in other circuits disregard the uncertainty created by the Sixth Circuit's holding and continue to provide location tax incentives (and if businesses, improbably, disregard that uncertainty and rely on those incentives), Ohio, Kentucky,

[6] Among other things, Kentucky grants companies that invest in economic development projects within qualified zones a 100% credit against the state income taxes that would otherwise be attributable to those projects. Ky. Rev. Stat. Ann. §§ 141.400, 154.45-010, 154.23-035. Michigan also grants tax credits to companies that make new investments within designated enterprise zones. Mich. Comp. Laws § 208.37(a). And Tennessee offers businesses a 1% excise tax credit for investments in industrial machinery within the State (Tenn. Code Ann. § 67-4-2009(4)(A)), as well as credits of $2,000 to $5,000 against franchise or excise tax liability for each net new full-time employee hired in Tennessee. Tenn. Code Ann. § 67-2-2109(B)(2). In an amicus brief filed in support of rehearing in the Sixth Circuit, these States represented that their various incentive programs overall had generated some $39 billion in investment from 1995 through 2002.

Michigan, and Tennessee will be disadvantaged in seeking to attract jobs and economic development that could be located elsewhere. This is a significant handicap to impose on States that rely on manufacturing and industry as a mainstay of their economies.

3. The Sixth Circuit's Ruling Conflicts With A Decision Of The Michigan Supreme Court

The uncertainty created by the decision below is especially acute because the Michigan Supreme Court, in *Caterpillar, Inc.* v. *Department of Treasury*, 488 N.W.2d 182 (Mich. 1992), *upheld* a state tax incentive that in relevant respects was quite similar to Ohio's ITC. The Michigan provision provided a capital acquisition deduction (the "CAD") from the State's Single Business Tax (a value-added type tax on business activity) for the acquisition of capital assets – but "only capital acquisitions related to Michigan business activity" benefited from the deduction. *Id*. at 186. See generally *Trinova Corp.* v. *Michigan Dep't of Treasury*, 498 U.S. 358, 385 (1991) (upholding the Single Business Tax against Commerce Clause challenge).

In particular, the CAD provided a deduction for the cost of acquiring real property, but only if "'the assets are physically located in Michigan.'" *Caterpillar*, 488 N.W.2d at 187 (citation omitted). Under this provision, "two otherwise similarly situated companies that invest in real property of equal value during the tax year will receive either a substantial deduction or no deduction at all, depending on whether that property is located in state or out of state." *Id*. at 203 (Cavanaugh, C.J., dissenting).[7] Michigan's CAD thus provided a

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[7] In addition, the CAD offered a deduction measured by the value of tangible personal property acquired by the taxpayer during the tax year. Although this deduction ostensibly was available no matter where the new tangible assets were located, it was calculated by multiplying the value of the newly acquired personal property by the average of two ratios: the ratio of the taxpayer's Michigan pay-

tax benefit for in-state business investment, while denying an equivalent benefit for equivalent business investment made out-of-state – just as does Ohio's ITC. Yet the Michigan Supreme Court had no difficulty finding the CAD constitutional under the Commerce Clause, explaining that the provision should not be regarded as discriminatory on its face because it "is available for any taxpayer" (*id*. at 192 (majority opinion)) and noting that the deduction did not have an impermissible purpose because the U.S. Supreme Court has "held that the promotion and development and investment of business in Michigan does not violate the Commerce Clause." *Ibid*. The court added that "a discriminatory effect does not result from fair encouragement of in-state business like that provided by [the CAD]." *Id*. at 193.

This conflict between the Michigan Supreme Court and the Sixth Circuit – the Circuit in which Michigan is located – will leave the law in a state of intolerable confusion if the court of appeals' decision stands. It creates unresolvable uncertainty about the constitutionality of tax incentives offered by states in the Circuit and invites forum shopping when such incentives are challenged. This consideration, too, warrants immediate review of the case by this Court.

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roll to its total payroll, and the ratio of the taxpayer's Michigan property to its total property. 488 N.W.2d at 186-187 (majority opinion). As a consequence of this formula, which makes the deduction more valuable as more of a taxpayer's property is located in-state, the inevitable effect of the personal property CAD was "that a greater deduction, resulting in a lower effective tax rate on the Michigan-apportioned tax base, is afforded * * * to * * * a company investing the new personal property in state, as opposed to a company investing the new personal property out of state." *Id*. at 202 (Cavanaugh, C.J., dissenting).

B. The Decision Below Departs From Principles Announced By This Court And Will Confuse Commerce Clause Doctrine

The need for review is particularly compelling because the Sixth Circuit's decision marks an extraordinary departure from any common-sense understanding of the Commerce Clause. Adopting what the plaintiffs themselves described below as a "novel legal theory" (No. 01-3960, *Cuno* v. *DaimlerChrysler Corp.* (6th Cir.), Pl. Br., at viii), the court of appeals struck down a law that was *not* designed to disadvantage interstate commerce, does *not* provide a meaningful competitive benefit to Ohio businesses vis-à-vis out-of-state competitors, does *not* disturb the flow of commerce across Ohio's borders – and *does* encourage the movement of business across state lines. In doing so, the court did not describe any articulable Commerce Clause policy that was advanced by its holding. Because that decision contributes to significant uncertainty about the scope of the Commerce Clause, intervention by this Court is called for.

1. There Is Uncertainty About The Application Of Commerce Clause Principles To Economic Development Tax Incentives

The outcome in the Sixth Circuit may be attributable to a degree of confusion in the law of the Commerce Clause as it relates to state economic development efforts. This Court has recognized that its analysis in this area "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." *Westinghouse Elec. Corp.* v. *Tully*, 466 U.S. 388, 403 (1984) (citations and internal quotation marks omitted). Commentators have agreed that there is "a palpable tension in the Supreme Court's decisions," marked by an "ill-defined distinction between the constitutional carrot and the unconstitutional stick in state tax, subsidy, and related cases." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 791-

792. See, *e.g.*, Clayton Gillette, *Business Incentives, Interstate Competition, and the Commerce Clause*, 82 MINN. L. REV. 447, 493 (1997) ("One point on which commentators agree is that our Commerce Clause jurisprudence is confused."). Indeed, "the Court has not had occasion to address a challenge grounded in the claim that a state tax provision's primary purpose or effect is to attract business to locate or expand in the state." Enrich, *supra*, 110 HARV. L. REV. at 381. In the absence of such clear guidance, respected commentators have divided on the constitutionality of provisions like the ITC. Compare Phillip M. Tatarowicz & Rebecca F. Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 VAND. L. REV. 879, 929-937 (1986) (such provisions are constitutional); Robert J. Firestone, *State Investment Tax Credits Do Not Violate the Dormant Commerce Clause*, 36 STATE TAX NOTES 189 (2005) (same); Gillette, *supra*, 82 MINN. L. REV. at 449 ("Locational incentives directed at business would appear, on their face, to serve the[] objectives of interstate competition."), with Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 817-825 (such provisions unconstitutional); Enrich, *supra*, 110 HARV. L. REV. 377 (same).

This disagreement perhaps is not surprising, because the question in cases like this one lies at the intersection of two competing Commerce Clause principles that point in very different directions. On the one hand, it is settled that the Clause precludes states from discriminating against out-of-state or interstate businesses, thus "avoid[ing] the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation." *Oklahoma Tax Comm'n* v. *Jefferson Lines, Inc.*, 514 U.S. 175, 180 (1995) (citations and internal quotation marks omitted).[8] On the other hand, however, the

[8] Under the test applied by this Court in *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977), a state tax satisfies the re-

Court has emphasized that "competition among the States for a share of interstate commerce is a central element of our free-trade policy." *Bacchus Imps., Ltd.* v. *Dias*, 468 U.S. 263, 272 (1984). As we explain below, we believe that the Sixth Circuit erred in where it struck the balance between these principles. But even if we are wrong in that submission, given the great uncertainty and confusion in the law – a confusion that has been significantly compounded by the Sixth Circuit's decision – guidance from this Court is urgently needed.

2. The Commerce Clause Proscribes Protectionist State Laws

Because the Commerce Clause's fundamental purpose was "'to keep commercial intercourse among the States free from all invidious and partial restraints'" (*Camps Newfound/Owatonna, Inc.* v. *Town of Harrison*, 520 U.S. 564, 571 (1997) (quoting *Gibbons* v. *Ogden*, 9 Wheat. 1, 231 (1824) (Johnson, J., concurring in the judgment)), the Clause has been understood to proscribe state laws that "discriminate[] against or unduly burden[] interstate commerce and thereby 'imped[e] free private trade in the national marketplace.'" *General Motors Corp.* v. *Tracy*, 519 U.S. 278, 287 (1997) (quoting *Reeves, Inc.* v. *State*, 447 U.S. 429, 437 (1980)). As the Court has explained, this anti-discrimination principle means that "the Commerce Clause prohibits economic protectionism – that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-

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quirements of the Commerce Clause if (1) the activity taxed has a substantial nexus with the taxing State; (2) the tax is fairly apportioned to reflect the degree of activity that occurs within the State; (3) the tax does not discriminate against interstate commerce; and (4) the tax is fairly related to benefits provided by the State. See also, *e.g.*, *Jefferson Lines*, 514 U.S. at 183. Plaintiffs do not deny that Ohio's ITC satisfies the first, second, and fourth prongs of this test. See App., *infra*, 4a.

state competitors." *Fulton Corp.* v. *Faulkner*, 516 U.S. 325, 330 (1996) (internal quotation marks and citations omitted). See, *e.g.*, *Camps Newfound/Owatonna*, 520 U.S. at 577-578; *Jefferson Lines*, 514 U.S. at 197 (1995); *Guy* v. *Baltimore*, 100 U.S. 434, 439 (1879).

In light of this purpose underlying the Clause, the "paradigmatic example of a law discriminating against interstate commerce is the protective tariff or customs duty, which taxes goods imported from other States, but does not tax similar products produced in State." *West Lynn Creamery, Inc.* v. *Healy*, 512 U.S. 186, 193 (1994). See Gerald Gunther & Kathleen Sullivan, CONSTITUTIONAL LAW 141 (13th ed. 1997) ("the national commerce power, it was hoped, would afford the means to end hostile state restrictions, retaliatory trade regulations, and protective tariffs on imports from other states"). While the Court has applied the Clause to many variations on that paradigm – for example, to laws that tax "'a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State'" (*Fulton Corp.*, 516 U.S. at 331 (quoting *Chemical Waste Mgmt., Inc.* v. *Hunt*, 504 U.S. 334, 342 (1992)), or that "discourage domestic corporations from plying their trades in interstate commerce" (*id*. at 333) – it has long been settled that the Clause is fundamentally directed at the use of state authority "with the aim and effect of establishing an economic barrier against competition with the products of another state or the labor of its residents." *Baldwin* v. *G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935). See, *e.g.*, *C & A Carbone, Inc.* v. *Town of Clarkstown*, 511 U.S. 383, 390 (1994) ("[t]he central rationale for the rule against discrimination is to prohibit state or municipal laws whose object is local economic protectionism"); *Exxon Corp.* v. *Governor of Maryland*, 437 U.S. 117, 126 (1978).

When state laws do not run afoul of this requirement – that is, when they do not impose a protectionist regime or penalize those who engage in interstate trade – nothing in the

Commerce Clause's antidiscrimination principle prevents the use of state tax statutes to provide incentives for in-state economic activity. Even while invalidating protectionist state laws, the Court has emphasized repeatedly that it did not mean to

> prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry. Nor do we hold that a State may not compete with other States for a share of interstate commerce; such competition lies at the heart of a free trade policy.

Boston Stock Exch., 429 U.S. at 336-337. The Court thus has stressed that "[t]he Commerce Clause does not prohibit all state action designed to give its residents an advantage in the marketplace." *New Energy Co.* v. *Limbach*, 486 U.S. 269, 278 (1988). To the contrary, "a State may enact laws pursuant to its police powers that have the purpose and effect of encouraging domestic industry." *Bacchus Imps.*, 468 U.S. at 271. See also, *e.g.*, *Trinova Corp.*, 498 U.S. at 385 (it 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").

In light of this principle, the Court has indicated that, for example, a state subsidy provided only to in-state companies "ordinarily imposes no burden on interstate commerce, but merely assists local business," even though such a regime obviously distinguishes between domestic and foreign enterprises. *West Lynn Creamery*, 512 U.S. at 199. See *id*. at 199 n.15; *New Energy*, 486 U.S. at 278 ("[d]irect subsidization of domestic industry does not ordinarily run afoul of [the Commerce Clause] prohibition"); Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 792 ("discriminatory subsidies * * * are almost always constitutional"); Dan T. Coenen, *Business Subsidies and the Dormant Commerce Clause*, 107 YALE L. J. 965 (1998) (same). And several Justices have declared that tax incentives may be equally permissible: the Commerce Clause does not "inhibit a State's power to experiment with different methods of encouraging local industry. Whether the encouragement takes the form of a cash subsidy, a tax credit, or a special privilege intended to attract investment capital, it should not be characterized as a 'burden' on commerce." *Hughes* v. *Alexandria Scrap Corp.*, 426 U.S. 794, 816 (1976) (Stevens, J., concurring). See *Chemical Waste Mgmt.*, 504 U.S. at 351 (Rehnquist, C.J., dissenting) ("[t]here seems to be nothing * * * that would prevent [a State] from providing subsidies or other tax breaks to domestic industries").

3. The Decision Below Finds No Support In This Court's Holdings

Against this background, the Sixth Circuit was wrong in its simplistic view that a state violates the Commerce Clause whenever its tax programs "further investment in-state at the expense of development in other states." App., *infra*, 9a. Indeed, the court of appeals' rule, if meant to be taken literally, cannot be correct. For example, it is universally agreed that states may cut their general tax rates to lure business from neighboring jurisdictions. See *West Lynn Creamery*, 512 U.S. at 199 n.15. Yet State A surely "furthers investment in-state at the expense of development in other states" in a very dramatic way when it lowers its corporate tax rates below those imposed by State B, both by making State A more attractive to business than State B and by giving corporate taxpayers in State A a competitive advantage over businesses that pay State B's higher rates. See generally *Ben Oehrleins & Sons & Daughter, Inc.* v. *Hennepin County*, 115 F.3d 1372, 1387 (8th Cir. 1997) (noting that companies may avoid states with "comparatively high state taxes"). The Sixth Circuit's rule accordingly cannot provide a sound basis for decision under the Commerce Clause.[9]

Nor does the holding below find support in the three decisions of this Court that were cited by the Sixth Circuit. See App., *infra*, 6a-9a (citing *Boston Stock Exchange*, *Maryland* v. *Lousiana*, 451 U.S. 725 (1981), and *Westinghouse Electric Corp.*). Those decisions certainly do not hold that it is impermissible for states to "further investment in-state at the expense of development in other states." And Ohio's ITC does not burden out-of-state transactions, activities, or actors, as was true of the laws challenged in each of the decisions relied upon by the court of appeals. Those laws "were really tariffs on interstate sales, manufacturing, or services," which involved straightforward attempts to benefit in-state firms at the expense of out-of-state competitors or to penalize the conduct of business in other states. Firestone, *supra*, 36 STATE TAX NOTES at 190. Ohio's ITC has no such effect.

In *Boston Stock Exchange*, the Court disapproved of a New York statute that, to protect the New York stock exchanges from out-of-state competitors, imposed a lower transfer tax on securities transactions completed through New York brokers than on identical transactions using out-of-state brokers. 429 U.S. at 324-325. Striking down the dif-

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[9] To reach its expansive holding, the court of appeals rejected what it characterized as the defendants' "view" that "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." App., *infra*, 9a. But as we have noted, that view is not something invented by the defendants in this case; using almost identical language, *this Court* has explained that "the Commerce Clause prohibits economic protectionism – that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors." *Fulton Corp.*, 516 U.S. at 330 (internal quotation marks and citations omitted).

ferential tax rate, the Court held "only that * * * no State may discriminatorily tax the products manufactured or the business operations performed in any other State." *Id*. at 336-337.

Similarly, in *Maryland* v. *Lousiana*, Louisiana imposed a tax on the "first use" of natural gas imported into the State that was identical in amount to the severance tax imposed on Louisiana gas producers. 451 U.S. at 731-733. But "exemptions and credits for the First-Use Tax" gave taxpayers subject to the levy a credit on any severance tax owed to Louisiana, while purchasers of gas used for consumption in the State were provided credits against other Louisiana taxes. *Id*. at 732-733. The result was that "Louisiana consumers of [out-of-state] gas for the most part [were] not burdened by the [First-Use] Tax." *Id*. at 733. The Court held that this regime "unquestionably discriminates against interstate commerce in favor of local interests" because "[c]ompetitive users in other States are burdened with the Tax" (*id*. at 756) while "Louisiana consumers of [out-of-state] gas are * * * substantially protected against the impact of the First-Use Tax." *Id*. at 757.

Finally, in *Westinghouse Electric Corp.*, the Court invalidated a New York law that taxed corporate income derived from subsidiaries engaged exclusively in export activity, but then awarded the parent company a partially offsetting tax credit that was dependent on the proportion of its total shipping activities that the subsidiary conducted in New York; the credit increased as the subsidiary "move[d] a greater percentage of its shipping activities into the State of New York" (466 U.S. at 400), and decreased as the firm increased its shipping activities in other states. As a result, the scheme "not only * * * 'provide[d] a positive incentive for increased business activity in New York State,'" "but also * * * penalize[d] increases in the [taxpayer's] shipping activities in other States." *Id.* at 400-401. The Court regarded this latter element as "the most pernicious effect of the credit scheme" because it "lower[ed] the incentive [the tax law] award[ed] for in-state * * * activity as the [taxpayer] increase[d] its out-of-state activity" (*id.* at 401 n.9), and therefore used "discriminatory state taxes to burden commerce in other States." *Id.* at 406.

The flaw in the New York scheme thus was its reliance "on *both* a taxpayer's in-state *and* out-of-state activities in determining the taxpayer's effective tax rate." Tatarowicz & Mims-Velarde, *supra*, 39 VAND. L. REV. at 929 (emphasis added). Indeed, after referring to "job-incentive credits" and "investment-tax credits," the Court specifically "reiterate[d] 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." 466 U.S. at 406 n.12 (emphasis added). "The clear implication" of this statement is that, absent an attempt to punish an increase in the taxpayer's out-of-state business, "investment tax credits and job incentive credits are *not* 'allowed on an impermissible basis' because they do not 'discriminatorily tax the products manufactured or the business operations performed in another state.'" Firestone, *supra*, 36 STATE TAX NOTES at 193 (emphasis added).

4. Ohio's ITC Is Consistent With Commerce Clause Principles

Given these holdings, the Sixth Circuit's decision "is not supported by existing case law and * * * the decision represents a significant and unwarranted expansion of the dormant Commerce Clause beyond its present scope." Firestone, *supra*, 36 STATE TAX NOTES at 189. See Biggins, *supra*, 14 J. MULTISTATE TAX'N & INCENTIVES at 37 (the Sixth Circuit's decision "is widely considered a departure from prior law"). In the Commerce Clause context, the Court has "eschewed formalism for a sensitive, case-by-case analysis of purposes and effects" (*West Lynn Creamery*, 512 U.S. at 201), with the outcome turning on "the unique characteristics of the statute at issue and the particular circumstances in each case." *Boston Stock Exch.*, 429 U.S. at 329. The Court has made clear that this "determination as to whether a tax incentive is coercive should depend on its 'practical or economic effect' and on 'economic realities.'" Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 811 (quoting *Goldberg* v. *Sweet*, 488 U.S. 252, 262 (1989) and *American Trucking Ass'ns, Inc.* v. *Scheiner*, 483 U.S. 266, 295 (1987)). And here, Ohio's ITC plainly is not a protectionist measure that was designed to help in-state businesses overcome out-of-state competitors; it does not penalize or otherwise impose burdens on out-of-state economic activity; and it establishes no requirements that disturb the free flow of commerce across Ohio's borders. Using the nuanced analysis of the statute's "purposes and effects" that is required by this Court's decisions, the credit accordingly does not run afoul of the Commerce Clause.

First, the credit plainly was not designed to give a competitive advantage to in-state taxpayers of the sort found problematic in *Boston Stock Exchange* and *Maryland* v. *Louisiana*. In those cases, states sought to benefit particular domestic industries by directly burdening out-of-state competitors with what amounted to protective tariffs. In contrast, Ohio confers no systematic advantage on in-state businesses, and does not in any way shield local industry from competition by out-of-state companies.

Indeed, many Ohio businesses will be unable to obtain the credit. Because the credit is available only to firms making new investments in the State that exceed the company's average investment over three baseline years, companies that confine their business to Ohio often will not qualify – but out-of-state firms making their first investment in Ohio *always* will qualify for the credit.[10] Thus, far from discouraging

[10] To qualify for a credit, any taxpayer (in-state or out-of-state) must make a new investment in Ohio. Thus, taxpayers that already engage in manufacturing in the state have no advantage over out-

interstate business, the Ohio credit encourages companies to operate across state lines. Needless to say, if every state had such a system, interstate businesses would not be systematically disadvantaged. To the contrary, all companies (local and interstate) would be eligible to obtain a tax credit of equal amount wherever they did business, and interstate firms would, if anything, be at an *advantage* because the preference given to new investment in the taxing jurisdiction would make such businesses far likelier to obtain the credit than would be companies that confined their operations to one state. See Gillette, *supra*, 82 MINN. L. REV. at 448 ("competition among states for businesses may actually facilitate the objective created by the Commerce Clause of achieving economic integration for the benefit of the nation as a whole"); Firestone, *supra*, 36 STATE TAX NOTES at 194 (Ohio's ITC "encourag[es] interstate commerce by burdening a sedentary local business"). Rather than conventional protectionist legislation, the credit thus is a permissible attempt to "encourage the growth and development of intrastate commerce and industry." *Boston Stock Exch.*, 429 U.S. at 336.

Second, the credit does not vary depending upon the percentage of its total business that a company conducts in Ohio, as did the statute invalidated in *Westinghouse Electric Corp.*, but instead focuses exclusively on the taxpayer's in-state activity. As two leading commentators have described the crucial distinction in this area,

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of-state taxpayers in obtaining the credit. As a practical matter, a business that has *no* current capital investment in Ohio can more easily qualify for the credit, because *any* initial investment it makes in the State will constitute an increase over its prior (zero) investment and thus will be eligible for a credit. By contrast, to receive a credit, a business that currently invests in a county would have to make an investment that exceeded its average investment in that county in the baseline years – and only the incremental or "excess" investment would qualify for any credit.

> 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 commerce clause is concerned. Rather, 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 and out-of-state activities in determining the taxpayer's effective tax rate. Such a provision clearly has a negative impact on interstate commerce.

Tatarowicz & Mims-Velarde, *supra*, 39 VAND. L. REV. at 928-929. In contrast, "[a] tax incentive that does not penalize out-of-state activity presumably could withstand scrutiny under the commerce clause after *Westinghouse*." *Id*. at 934. And here, the Ohio credit satisfies this test. Unlike the tax credit in *Westinghouse*, the same credit is available regardless of the extent of the taxpayers' overall presence in the state, and the amount of the credit is not reduced as the taxpayer increases its investment in other states.

Third, the activity that benefits from the Ohio credit (capital investment) is not itself subject to state tax. That stands in sharp contrast to the situation in the cases where the Court invalidated tax incentives as discriminatory; in *Boston Stock Exchange* and *Maryland* v. *Lousiana*, the domestic activities that the states sought to encourage were themselves subject to tax, and the states encouraged these activities by discriminatorily relieving domestic taxpayers of a portion of the tax. See Firestone, *supra*, 36 STATE TAX NOTES at 191, 192. That approach resulted in the systematic differential taxation of particular types of interstate commerce in a manner that burdened out-of-state competitors. Here, however, the ITC is not an exemption that lowers the effective rate of taxation on a particular activity, but is instead a one-time, bottom line subtraction from a tax that Ohio was entitled to collect. That subtraction is designed to encourage conduct (capital investment) that differs from the taxed activity (the production of income within the State). As such, it is the precise equivalent of direct spending by the State on, for example, construction of roads to a new plant – spending that might substantially lower the cost of developing the facility, but that plainly would not violate the Commerce Clause. See Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 835 ("[e]conomists know that the real-world impact of such a subsidy mirrors the effect of the credit") (footnote omitted).

To be sure, the Court has drawn a distinction between subsidies for domestic commerce, which "ordinarily" are permissible (*New Energy*, 486 U.S. at 278), and tax exemptions, which in some circumstances have been held invalid. See *Camps Newfound/Owatonna*, 520 U.S. at 588-591. But the Court has indicated that "this distinction [between subsidies and tax benefits] is * * * applicable to claims that certain state action [is] *designed to give residents an advantage in the marketplace*." *Id*. at 590 (emphasis added). And in this case, where the State's credit is a one-time benefit for engaging in particular activity that is *not* designed to offer a systematic advantage to domestic businesses over out-of-state competitors, the credit's similarity to a subsidy should be decisive. "From a constitutional perspective, it is often compelling to view such one-time, targeted tax benefits as akin to direct expenditures rather than as part of the same category occupied by paradigmatic tax benefits." Edward A. Zelinsky, *Are Tax "Benefits" Constitutionally Equivalent to Direct Expenditures?*, 112 HARV. L. REV. 379, 409 (1998). Cf. *Westinghouse Elec. Corp.*, 466 U.S. at 405 (Court has "declined to attach any constitutional significance to such formal distinctions that lack economic substance").

This is not to say, of course, that all subsidies and tax exemptions must be equated for Commerce Clause purposes. Instead, our point is that a particular kind of tax credit – one that is available for engaging in one-time, non-repetitive business activity, and that does not give in-state businesses any continuing competitive advantage over out-of-state firms – is precisely equivalent to a direct subsidy. Nothing in this

Court's decisions, which repeatedly emphasize that Commerce Clause analysis must turn on "the unique characteristics of the statute at issue and the particular circumstances in each case" (*Boston Stock Exch.*, 429 U.S. at 329), suggests that this kind of functional parallel between related tax and subsidy programs is inappropriate.

5. The Decision Below Actually Discourages Interstate Business

At bottom, the controlling question here is whether the credit is a permissible attempt to encourage domestic industry rather than illegitimate protectionism. In answering that question, it is revealing that the plaintiffs here are *not* out-of-state entities who pay the challenged tax, competitors of taxpayers who obtain favorable tax treatment, or customers of entities that are handicapped by discriminatory taxes. Far from it: DaimlerChrysler's competitors vigorously *support* the constitutionality of Ohio's ITC. Instead, the plaintiffs here are, for the most part, residents of the taxing State who would like Ohio to collect *more* tax from out-of-state companies doing business in the State.

This is an exceedingly strange use of the Commerce Clause. Even critics of location tax incentives recognize that such provisions

> are quite different from the more familiar targets of Commerce Clause attacks, which, like tariffs, either protect local businesses from multistate competitors or extract tax revenues disproportionately from out-of-state businesses. Whereas the out-of-state challenger to these sorts of provisions can convincingly claim that the state unfairly excluded or penalized outsiders, such pleas are far less compelling when the challenged provision is designed to invite, even to entice, the outsiders in.

Enrich, *supra*, 110 HARV. L. REV. at 412. After all, the whole point of the Commerce Clause anti-discrimination principle is "creating a level playing field between the taxpayer and its in-state competitors. * * * Indeed, it is this consequence of invalidating the tax incentive that provides the essential justification for judicial intervention under the dormant Commerce Clause." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 872.

But there is no such justification in this case, where local residents have invoked the Clause to prevent their State from giving a break to an out-of-state taxpayer that is engaged in interstate commerce. Here, "competition would not be served by eliminating any tax differential * * *, and the dormant Commerce Clause has no job to do." *General Motors Corp.*, 519 U.S. at 303. Because none of the concerns that animate the Clause are implicated here, there is no basis for the Sixth Circuit's decision to strike down one of Ohio's principal tools for attracting jobs and fostering economic development. And because that decision has profoundly important national consequences, review of the decision below by this Court is warranted. The Court accordingly should grant the petitions filed by DaimlerChrysler and the State of Ohio challenging the Sixth Circuit's decision that the ITC is unconstitutional.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted.

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