Nos. 04-1704 and 04-1724

In The
Supreme Court of the United States

DAIMLERCHRYSLER CORP.,

Petitioner,

v.

CHARLOTTE CUNO, et al.,

Respondents.

AND

WILLIAM W. WILKINS, Tax Commissioner etc., et al.,

Petitioners,

v.

CHARLOTTE CUNO, et al.,

Respondents.

On Writs Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

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INTRODUCTION

Recent years have seen a rapid proliferation of state and local tax breaks targeted to businesses that agree to locate in the state or locality. Ohio's two tax provisions that are challenged in this case, an investment tax credit against its corporate franchise tax and an exemption from personal property taxes for businesses that commit to specified local levels of investment and employment, are characteristic examples of this national trend. To the limited extent that such tax breaks actually affect business location decisions, they distort the free flow of investment in an open national economy. In fact, they only have minimal impacts on business decisions, largely because most jurisdictions offer comparable breaks. Nonetheless, they impose high costs on states and localities in lost tax revenues. The states are caught in a classic prisoners' dilemma which leaves all of them, their citizens who pay taxes and depend on services, and the national economy, all worse off.

This trend is the most recent iteration of one of the dangers that led to the enactment of the Commerce Clause. From experience with interstate trade rivalries under the Articles of Confederation, the Framers recognized the need for national controls so that the states would not seek to improve their parochial positions by taxation and regulation that advantaged in-state economic activity. Respondents seek to enforce this basic constitutional constraint on state taxation and to protect themselves and others from the injuries flowing from the states' escalating rivalry to enact discriminatory tax preferences favoring in-state business location. By upholding the Sixth Circuit, this Court can reaffirm its longstanding prohibition against discriminatory state taxation and guide state tax policy away from this most recent slide toward "economic Balkanization." *Hughes v. Oklahoma*, 441 U.S. 322, 325 (1979).

STATEMENT OF THE CASE

Respondents filed this Commerce Clause challenge in the Ohio state courts in March, 2000, against two tax incentive programs used by Ohio and the City of Toledo to induce DaimlerChrysler ("Daimler") to build a new Jeep assembly plant in Toledo, where the old plant had also been. *See* Compl., Joint Appendix ("J.A.") at 24a, 29a. One incentive is a ten-year exemption from personal property taxes levied by Toledo and the school districts in which the plant is located, an exemption that was conditioned on the company agreeing to provide specified levels of jobs and investment at the plant. The other incentive is an investment tax credit ("ITC") against Ohio's corporate franchise tax, an income tax levied on the fraction of a corporation's net income that is apportioned to Ohio based on the percentages of the corporation's property, payroll and sales that are situated in Ohio.[1] The ITC reduces this tax based on a corporation's qualifying investment in machinery and equipment installed in Ohio, and thereby discriminates in favor of businesses locating new investment in the state and against those locating elsewhere.[2]

These two tax breaks are costing the state, the city, and the school districts many millions of dollars in lost revenues. In the Daimler agreement alone, they were the primary elements of a $280 million incentives package.

[1] Ohio's statutory apportionment formula deviates from the traditional three-factor formula by assigning the sales factor three times the weight of the other factors. *See* Br. for Pet'r Ohio ("St. Br.") 7.

[2] As is noted in St. Br. 6 n.3, Ohio's statute providing for its ITC has been recently amended, *see* Ohio Rev. Code Ann. ("O.R.C.") § 5733.33(B)(1), as amended by 2005 Ohio Laws 28 § 101.02, but Respondents agree with the State that the replacement provision, O.R.C. § 122.173, continues to provide Daimler and other beneficiaries of the ITC with tax breaks that are, for purposes of constitutional analysis, functionally equivalent.

See App. to Pet. for Writ of Cert., *DaimlerChrysler Corp. v. Cuno*, No. 04-1704 ("Pet. App.") at 2a. Ohio estimates that its ITC causes a revenue loss of more than $120 million annually, *see* State of Ohio, Exec. Budget, Fiscal Yrs. 2006 & 2007, Bk. Two – Tax Expenditure Budget 26 (Feb. 2005), and the losses from any particular project extend for seven to ten years. St. Br. 9. The property tax exemption program was estimated to cause annual revenue losses of $13.7 million for the Toledo school district alone, seriously impairing the district's ability to fulfill its educational mission. Robert Tomsho, *In Toledo, A Tension Between School Funds and Business Breaks*, WALL ST. J., July 18, 2001, at A1. Statewide, the property tax exemption costs school districts more than $100 million annually. National Educ. Ass'n, Protecting Public Education From Tax Give-aways to Corporations 19 (2003). These lost revenues significantly deplete the state and local resources to which Respondents contribute through their own taxes and on which they rely for essential services.[3]

In the interstate competition for business, most other states have adopted similar tax breaks, and the cumulative costs nationally are staggering. Despite overwhelming empirical evidence for the limited efficacy of such incentives,[4] some 37 states have adopted ITCs similar to Ohio's.

[3] As is detailed below, a portion of Ohio's corporate franchise tax is automatically distributed, by statutory formula, to local governments. Hence, Ohio's ITC directly depletes the resources of both state and local governments.

[4] *See, e.g.,* Ohio Economic Development Study Advisory Committee, *An Assessment of the Costs, Benefits, and Overall Impact of the State of Ohio's Economic Development Programs, Final Report* 171 (May 1999) (finding that Ohio's ITC "had little positive impact on the Ohio economy as measured in terms of jobs, gross state product, and personal income"); California Legislative Analyst's Office, *An Overview of California's Manufacturers' Investment Credit* 11 (Oct. 2002) (similar);
(Continued on following page)

See Pet. for Writ of Cert., *Wilkins v. Cuno*, No. 04-1724 ("St. Pet.") 22 n.5. The annual cost of these ITCs in the handful of states for which estimates are available comes to $844 million. *Id*. at 25. Likewise, virtually every state offers targeted property tax exemptions for businesses, many of which, like Ohio's, are conditioned on specified levels of in-state investment or employment;[5] the annual cost of just one state's exemption program will exceed $400 million by 2008, *see* Tex. Tax Expenditure and Incidence Report 2005-2007, Table 1 at 36 (2003). The inevitable result is a significant shift of the costs of state and local government to other classes of taxpayers, like Respondents, and a substantial reduction in states' and localities' ability to deliver important public services. *See, e.g.,* Peter Fisher, *Tax Incentives and the Disappearing State Corporate Income Tax*, 2002 ST. TAX TODAY 42-1 (March 4, 2002).

Respondents include individual and small business taxpayers from Toledo. *See* Compl., J.A. at 18a-19a. They brought suit in the Ohio state courts, and Petitioners removed the case to the Northern District of Ohio. Respondents promptly moved to remand, largely because they were concerned that the federal courts might find they lacked standing. In particular, they feared the prospect of extended litigation on the merits of their claims in the federal courts, only to be told, years later, that they must start over in state court. *See* Pl. Reply in Supp. of Mot. to Remand 10 (July 27, 2000). Respondents argued that the district court should remand the case to the Ohio state courts, where the rules for citizen/taxpayer standing

see generally ROBERT G. LYNCH, RETHINKING GROWTH STRATEGIES 25-36 (2004).

[5] *See* Esteban G. Dalehite, et al., *Variation in Property Tax Abatement Programs Among States*, 19 ECON. DEV. Q. 157 (2005); National Educ. Ass'n, *supra*, at 11.

are less restrictive.[6] Petitioners argued in response that "plaintiffs *do* have standing to proceed in federal court," on the very theories that they attack in their present briefs. Daimler Mem. in Opp. to Pl. Mot. to Remand 14 (July 17, 2000) (emphasis in original). In November 2000, the court denied the motion to remand, finding that the court had jurisdiction over Respondents' claims under principles of municipal taxpayer standing. *See* J.A. at 78a (citing *Massachusetts v. Mellon*, 262 U.S. 447 (1923)).

Over the next four years, as the lower courts addressed the merits, the issue of standing was not raised again by either Petitioners or any judge. In August 2001, the district court granted Petitioners' motions to dismiss the complaint, concluding that neither challenged tax break discriminated between in-state and out-of-state activity in a manner that violated the Commerce Clause. Respondents appealed, and in October 2004 the Sixth Circuit reversed the decision on the constitutionality of Ohio's ITC, but affirmed the ruling on the property tax exemption. About the ITC, the court of appeals reasoned, by analogy to a long line of Supreme Court cases, that the state, by granting tax credits to businesses that are subject to Ohio's franchise tax if they locate new economic activity at sites in Ohio while denying the credits to identically situated businesses that locate new activity out of state, was discriminating in favor of in-state economic activity, in a manner "wholly inconsistent with the free trade purpose of the Commerce Clause." Pet. App. at 7a

[6] *See, e.g., State ex rel. Ohio Acad. of Trial Lawyers v. Sheward*, 715 N.E.2d 1062, 1082-83 (Ohio 1999) (recognizing citizen standing to address issues of "great importance and interest to the public"); *Clay v. Harrison Hills City Sch. Dist. Bd. of Educ.*, 723 N.E.2d 1149, 1153-54 (Ohio Com. Pl. 1999) (recognizing taxpayer standing based on state constitutional grant of access to the courts).

(quoting *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 336 (1977)). The court explained that

> any corporation currently doing business in Ohio, and therefore paying the state's corporate franchise tax in Ohio, can reduce its existing tax liability by locating significant new machinery and equipment within the state, but it will receive no such reduction in tax liability if it locates a comparable plant and equipment elsewhere. Moreover, as between two businesses, otherwise similarly situated and each subject to Ohio taxation, the business that chooses to expand its local presence will enjoy a reduced tax burden, based directly on its new in-state investment, while a competitor that invests out-of-state will face a comparatively higher tax burden because it will be ineligible for any credit against its Ohio tax.

Pet. App. at 6a. By contrast, the court held the property tax exemption did not unconstitutionally discriminate against interstate commerce, because the specific terms imposed as conditions on the exemptions were "minor collateral requirements . . . directly linked to the use of the exempted . . . property." *Id.* at 12a.[7]

Both Petitioners sought rehearing of the Sixth Circuit's decision. In Ohio's petition, but not Daimler's, it argued for the first time that Respondents lacked standing. Ohio Pet. for Reh'g 2 (Sept. 16, 2004). When the Sixth

[7] The Sixth Circuit provided no explanation for characterizing the conditions imposed by the Ohio program as "minor" or "collateral," and it offered neither explanation nor authority for its view that conditions "directly linked to the use of the exempted . . . property" did not unconstitutionally discriminate against interstate commerce, despite the fact that this Court, in *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997), had struck down precisely such a condition. Respondents' petition for review of the property tax exemption ruling remains pending. *Cuno v. DaimlerChrysler Corp.* (No. 04-1407).

Circuit declined to rehear the case, Petitioners sought review of the ITC ruling in this Court, but raised no questions about standing or the federal courts' jurisdiction over the case. Only after this Court directed the parties to brief standing have Petitioners taken up the argument that Respondents should be required to start over again in the state courts where they sought to conduct the litigation in the first place.

SUMMARY OF ARGUMENT

1. Respondents are taxpayers of Ohio and Toledo, the two jurisdictions losing revenue from the ITC and property tax exemptions challenged in this case as violations of the Commerce Clause. They claim standing here in their capacities as state and municipal taxpayers, the standards for both of which, lower courts agree, are less difficult to satisfy than those for federal taxpayers. This Court has held that taxpayers can meet the requirements of Article III standing in some cases, including those in which the tax revenues are federal and in which the loss suffered was due to an expenditure (to support religious schools) that the Constitution prohibits, even where there was no showing that any taxpayer would have paid less taxes and/or received other benefits from the federal government if the challenged expenditures were set aside. *Flast v. Cohen,* 392 U.S. 83 (1968). The fact that *some* plaintiffs have standing to assert *some* federal claims based solely on their status as taxpayers demonstrates that Article III does not present an absolute barrier to upholding standing in this case. Rather, the question is whether prudential considerations should bar this Court from reaching the merits of the Sixth Circuit rulings.

There are three reasons why Petitioners' belated standing arguments should be rejected. First, Respondents should be found to have standing in their capacity as state taxpayers to challenge a state law which unconstitutionally diminishes state tax revenues to the detriment of all the state's taxpayers. Even if the standards for state taxpayer standing are as stringent as those for federal taxpayers, standing is appropriate where the taxpayers' challenge has a sufficiently close nexus to their taxpayer status and rests on a constitutional provision, such as the Commerce Clause, which directly limits the states' taxing powers. *See Flast*, 392 U.S. at 102-03. Second, Respondents should be found to have standing in their capacity as municipal taxpayers, both because a substantial part of Ohio's franchise tax, whose revenues are depleted by the challenged ITC, is automatically transferred to local governments like Toledo, and because Respondents' municipal taxpayer standing to challenge the property tax exemptions in the Daimler agreement should extend to the entire case or controversy, of which the challenge to the ITC is an integral part. *See* 28 U.S.C. § 1367.

Finally, because the potential obstacles to the federal courts' jurisdiction in this case are prudential, and not constitutional, a wide range of factors peculiar to this case – the fact that defendants, not plaintiffs, invoked the jurisdiction of the federal courts; the efforts of plaintiffs to raise the issue of standing and have the case remanded to the state courts at the outset; the absence of any challenge to standing, by either defendants or the lower courts, in the years of litigation leading up to the Circuit Court's decision; the difficulty and novelty of the questions of state and municipal taxpayer standing; and the absence of an appellate court opinion on the application of those doctrines to these claims – suggest the desirability of upholding standing in the interests of "finality, efficiency, and economy," in the special circumstances of this case. *See Caterpillar, Inc. v. Lewis*, 519 U.S. 61, 75 (1996).

2. The Ohio ITC is a paradigm of a state tax provision which facially discriminates against interstate commerce by providing a direct advantage to in-state activity.

Because the ITC is only available for in-state investments in machinery and equipment, it allows those businesses which locate in the state to pay a lower tax to Ohio than their otherwise identically situated competitors with identical Ohio taxable income but who locate elsewhere. Such "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter" has long been recognized to be "virtually *per se* invalid" under the Commerce Clause. *Oregon Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 99 (1994).

Petitioners seek to avoid this conclusion by several flawed arguments. First, because Ohio's chosen apportionment formula (which determines the share of a multistate business's income that is subject to Ohio tax) attributes to Ohio more of the income of businesses locating new investment in-state than of similar businesses locating out-of-state, they contend that the ITC merely reduces the additional tax burden on in-state businesses and does not discriminate between similarly situated businesses. But this contention ignores the fact that, due to the ITC, the in-state company will pay a lower effective tax rate than its out-of-state competitor on the portion of income that Ohio has identified, under its presumptively fair apportionment rules, as subject to Ohio tax. So, it fails the very test previously applied by this Court in comparable circumstances. *See Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388 (1984).

In addition, unable to identify a single case in which this Court has upheld a measure that provided preferential tax treatment conditioned on in-state economic activity, Petitioners offer several novel reinterpretations of the Court's Commerce Clause cases in an effort to distinguish Ohio's ITC from the numerous preferential provisions struck down by the Court. These restrictive reinterpretations depend on drawing a sharp distinction between tax measures which benefit in-state activity and those which penalize out-of-state activity, a distinction the Court has repeatedly rejected, and one which can neither account for the Court's precedents nor further the Commerce Clause's central purposes. Nor are these restrictive reinterpretations necessary, as Petitioners contend, to preserve the states' autonomy to shape their tax systems or to devise other public policies that encourage local economic development. The states already have available a wide array of non-discriminatory tax and non-tax pro-development policies, such as lowering tax rates or improving infrastructure and schools, that face no danger from the Court's Commerce Clause jurisprudence.

ARGUMENT

I. Respondents have standing to maintain this Commerce Clause challenge.

A. Respondents have standing as state taxpayers to challenge tax measures that are claimed to violate the Commerce Clause.

This Court has had a number of opportunities in recent years to address the scope of federal taxpayers' standing, *see, e.g., Bowen v. Kendrick*, 487 U.S. 589 (1988); *Valley Forge Christian Coll. v. Americans United for Separation of Church & State*, 454 U.S. 464 (1982). In those cases, it has identified a circumscribed set of conditions under which federal taxpayers have standing. *See, e.g., Bowen*, 487 U.S. at 618-20; *Flast v. Cohen*, 392 U.S. 83, 101-03 (1968). By contrast, the last case in which the Court issued a decision on state taxpayer standing was *Doremus v. Board of Education*, 342 U.S. 429 (1952), where the challenged governmental action – requiring daily Bible reading in the state's schools – was not alleged to have any impact on the state's revenues and thus could not ground any claim of taxpayer standing. *See also ASARCO Inc. v. Kadish*, 490 U.S. 605, 613-14 (1989)

(Kennedy, J., plurality opinion) (suggesting, in *dicta*, that state taxpayers are "likened . . . to federal taxpayers").

Absent more definitive guidance, the lower courts have adopted a range of approaches to questions of state taxpayer standing, with some applying the more liberal standards applicable to municipal taxpayers, *see, e.g., Arakaki v. Lingle*, 423 F.3d 954, 967-69 (9th Cir. 2005); *Johnson v. Econ. Dev. Corp.*, 241 F.3d 501, 508 (6th Cir. 2001) (equating municipal and state taxpayers as "nonfederal taxpayers" for standing purposes), while others use the stricter standards applicable to federal taxpayers, *see, e.g., Board of Educ. v. N.Y. St. Teachers Ret. Sys.*, 60 F.3d 106, 110 (2d Cir. 1995); *Colo. Taxpayers Union, Inc. v. Romer*, 963 F.2d 1394, 1402 (10th Cir. 1992). The leading treatise concludes, "When viewed from the perspectives of current standing doctrine, state taxpayer standing is more likely to seem plausible than federal taxpayer standing." 13 C. WRIGHT, A. MILLER, & E. COOPER, FEDERAL PRACTICE & PROCEDURE § 3531.10 (2d ed. 1988); *see also* Nancy C. Staudt, *Modeling Standing*, 79 N.Y.U. L. REV. 612, 632 (2004) (describing state taxpayers as "subject to something like 'intermediate scrutiny'").

In the present case, however, it is unnecessary to resolve the question of whether state taxpayers should be treated more hospitably than federal taxpayers. Even in the case of federal taxpayers, the Court has found standing where there is a sufficiently close nexus between the plaintiffs' taxpayer status and the claims that they assert. *See, e.g., Bowen, supra*; *Flast*, *supra*. Federal taxpayer claims must pass two tests. First, "the taxpayer must establish a logical link between that status and the type of legislative enactment attacked," *Flast*, 392 U.S. at 102, a link that is satisfied, in the federal taxpayer context, when the challenge is directed to an exercise of Congress's taxing and spending power. *See, e.g., Valley Forge*, 454 U.S. at 478. Second, "the taxpayer must establish a nexus between that status and the precise nature of the constitutional infringement alleged," *Flast*, 392 U.S. at 102, a requirement that is met, in the federal context, when the suit rests on a constitutional provision that is a specific limitation on the exercise of the taxing and spending power, *id.* at 103.

State taxpayer claims like this one, asserting Commerce Clause challenges to state tax breaks, straightforwardly satisfy both *Flast* standards and hence should be allowed, even if the standards for state taxpayers are fully as restrictive as those for federal taxpayers. With regard to the first requirement, the legislative enactment challenged in the case, a credit against a state tax, is unquestionably an exercise of the state's taxing power, precisely analogous to exercises of the taxing power that satisfy *Flast*'s first prong. *See, e.g., Sch. Dist. v. Ball*, 473 U.S. 373, 380 n.5 (1985) (citing with approval the application of *Flast* standing for a taxpayer challenge to a state tax exemption in *Hunt v. McNair*, 413 U.S. 734 (1973)); *Johnson*, 241 F.3d at 507-08. *Cf. Hibbs v. Winn*, 542 U.S. 88, 110-12 (2004) (citing with approval the granting of jurisdiction in Establishment Clause challenges to state tax credits, deductions and exemptions). The grant of a state tax credit – as opposed, for instance, to a regulatory statute involving only "an incidental expenditure of tax funds," *Flast*, 392 U.S. at 102 – relates directly to a state taxpayer's interest qua taxpayer and causes a direct injury to that interest. The effect of the tax credit is to deplete the state coffers to which Respondents (individual and small business taxpayers) must contribute through their own tax obligations, with the result that either their contributions must be increased or the sum total available to fund programs on which they rely is diminished.

With regard to *Flast*'s second requirement, in cases involving federal taxpayer standing, only the Establishment Clause has been recognized as a "specific constitutional limitation[ ]," *id.* at 102-03, on the taxing and spending power. Its special status rests on its special historical role. As the Court explained,

> Our history vividly illustrates that one of the specific evils feared by those who drafted the Establishment Clause . . . was that the taxing and spending power would be used to favor one religion over another or to support religion in general.

Id. at 103. In the case of the states' taxing powers, another constitutional provision – the Commerce Clause – has played a similar historical role, as a specific limit on discriminatory state taxation. Indeed, the central purpose of the Commerce Clause was to curb inappropriate state tax measures. "Under the Articles of Confederation, state taxes and duties hindered and suppressed interstate commerce; the Framers intended the Commerce Clause as a cure for these structural ills." *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992) (citing *The Federalist* Nos. 7 & 11 (Alexander Hamilton)). And, just as James Madison explicated the crucial role of the Establishment Clause in preventing the improper use of governmental taxing and spending powers to aid religions, *see Flast*, 392 U.S. at 103-04, he likewise explained that the 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." *West Lynn Creamery v. Healy*, 512 U.S. 186, 193 n.9 (1994) (quoting letter from James Madison to J.C. Cabell (Feb. 13, 1829)).

In each case, the function of the constitutional provision is to prevent the government from providing special benefits to favored constituencies in ways that imperil the common good, *see, e.g., Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 299 (1997) (noting "the dormant Commerce Clause's fundamental objective of preserving a national market for competition undisturbed by preferential advantages conferred by a State upon its residents or resident competitors"), and, in each case, the taxing and spending powers pose a significant threat of such favoritism.[8] In each case, the harm to be avoided by these fundamental protections is the loss of governmental neutrality, whether in the competition among religions or among in-state and out-of-state businesses, more than governmental intrusion on the rights or liberties of particular individuals or firms.[9] And in each case, the damage caused by violations of the provisions is, in large part, broadly diffused among all who contribute to government and depend on its benefits, but who are not benefitted by the forbidden special treatment. Indeed, in the Commerce Clause context, the Court has identified the "loss of specific tax revenues" as a type of injury against which the clause protects and as a permissible basis for standing, at least in the context of a suit brought by one state against another. *See Wyoming v. Oklahoma*, 502 U.S. 437, 447-448 (1992).

[8] Both Establishment Clause and Commerce Clause can also be violated by regulatory measures, but taxpayer standing is not ordinarily available to challenge such measures. *See Flast*, 392 U.S. at 102 (distinguishing *Doremus*). The Commerce Clause is also, of course, an affirmative, but limited, grant of power to Congress. *See, e.g.*, *United States v. Lopez*, 514 U.S. 549 (1995). But this aspect of the Commerce Clause is not a specific limit on Congress's taxing and spending power, and hence taxpayer standing would not extend to cases questioning exercises of Congress's Commerce Clause authority. *Cf. Flast*, 392 U.S. at 104-05.

[9] *Compare Engel v. Vitale*, 370 U.S. 421, 430-31 (1962) ("The Establishment Clause, unlike the Free Exercise Clause, does not depend upon any showing of direct governmental compulsion and is violated by the enactment of laws which establish an official religion whether those laws operate directly to coerce nonobserving individuals or not.") *with Quill*, 504 U.S. at 312 (observing that the Commerce Clause, as distinct from the Due Process Clause, is informed "not so much by concerns about fairness for the individual . . . as by structural concerns about the effects of state regulation on the national economy").

Thus, just as taxpayers (federal, state, and local) have standing to challenge taxing and spending that is alleged to violate the Establishment Clause's guarantee of neutrality in matters of religion, so state taxpayers should be found to have standing to challenge measures claimed to violate the Commerce Clause's core neutrality principle that no State "may impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business." *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 329 (1977).

B. Respondents have standing as municipal taxpayers.

While there is uncertainty regarding the scope of state taxpayer standing, the courts have consistently viewed municipal taxpayers far more permissively than federal taxpayers. *See, e.g., Donnelly v. Lynch*, 691 F.2d 1029 (1st Cir. 1982); Nancy C. Staudt, *Taxpayers in Court: A Systematic Study of a (Misunderstood) Standing Doctrine*, 52 EMORY L.J. 771, 803 (2003) ("A presumption in favor of municipal taxpayer standing exists."). Federal courts have consistently acknowledged that municipal taxpayers have a more direct and immediate relationship to their communal fisc than state or federal taxpayers. Thus, "[w]hen a municipal taxpayer can establish that the challenged activity involves a measurable appropriation or loss of revenue, the injury requirement is satisfied." *D.C. Common Cause v. Dist. of Columbia*, 858 F.2d 1, 5 (D.C. Cir. 1988); *see, e.g., Hawley v. City of Cleveland*, 773 F.2d 736 (6th Cir. 1985); *United States v. City of New York*, 972 F.2d 464 (2d Cir. 1992).

This Court articulated the presumption of municipal taxpayer standing in *Frothingham v. Mellon*, 262 U.S. 447, 486 (1923) ("the interest of a taxpayer of a municipality in the application of its moneys is direct and immediate").

Since *Frothingham*, the Court has not revisited whether municipal taxpayers should be held to a different standard than state and federal taxpayers, but the lower courts have consistently preserved the distinction. *See City of New York*, 972 F.2d at 471 ("courts of appeals . . . have uniformly concluded that municipal taxpayers have standing to challenge allegedly unlawful municipal expenditures"). *Cf. ASARCO*, 490 U.S. at 613 (Kennedy, J., plurality opinion) (acknowledging, in *dicta*, the continuing validity of a distinction between municipal and federal taxpayers.) In the present case, Respondents have standing as municipal taxpayers because both the ITC and the property tax exemption directly reduce the revenues of the local governments to which Respondents pay taxes.

By operation of Ohio law, a portion of the state's franchise tax is automatically distributed to localities. Pursuant to O.R.C. § 5733.12, 4.2% of franchise tax revenue is allotted to the "Local Government Fund" and 0.6% to the "Local Government Revenue Assistance Fund." The sums in these two funds are then allocated to local governments pursuant to complex statutory formulae, *see* O.R.C. §§ 5747.50, 5747.61. Under these formulae, in 2003, approximately 4.3% of the amounts credited to the Funds was distributed to local entities to whom Respondents pay taxes.[10] Hence, of some $120 million in franchise tax revenues lost annually due to the ITC, about $250,000 (i.e., $120 million x 4.8% x 4.3%) represents revenues lost by local government units to which Respondents pay taxes, thereby injuring them materially in their municipal taxpayer role.

[10] *See* Ohio Dep't of Taxation, Annual Report 2004 at 94-95 (available at http://tax.ohio.gov/divisions/communications/publications/annual_reports/publications_annual_report_2004.stm).

Of course, the loss of revenue at the local level due to the ITC is the result of a state law, and not primarily the work of the local government. The clearest case of municipal taxpayer standing is one in which the municipality itself has mishandled the funds of its resident taxpayers. However, courts have recognized that municipal taxpayer standing depends on the damage to the municipal fisc, and not on the particular government actor who has caused the loss. *See*, *e.g.*, *Banner v. United States*, 428 F.3d 303, 307 n.5 (D.C. Cir. 2005); *Gwinn Area Cmty. Sch. v. Michigan*, 741 F.2d 840, 844 (6th Cir. 1984); *Cammack v. Waihee*, 932 F.2d 765, 770-71 (9th Cir. 1991).

Even if Respondents do not have municipal taxpayer standing based solely on their ITC claim, they had – and continue to have – standing as municipal taxpayers to challenge the property tax exemption in federal court. In the district court, Daimler conceded that plaintiffs had standing as municipal taxpayers to challenge the property tax exemption. *See* Daimler Mem. in Opp. to Pl. Mot. to Remand 14-17. This situation presents the paradigmatic example of municipal taxpayer standing, where the City has acted in a manner that depletes the municipal fisc. *See*, *e.g.*, *Hawley,* 773 F.2d at 741; *City of New York*, 972 F.2d at 470-71. Here, Toledo has relieved Daimler from its obligation to pay personal property taxes, thereby reducing the city's tax revenue. As Toledo taxpayers, Respondents are directly injured by the City's action.

Even if Respondents' status as municipal taxpayers only applies to their challenge to the property tax exemptions, their standing with respect to that aspect of the case satisfies the minimum requirement that the district court had proper jurisdiction over at least some claims in the case when it was removed. And, once the requirement of a "civil action . . . of which the district courts of the United States have original jurisdiction" has been met, 28 U.S.C. § 1441(a), the district court properly exercised its jurisdiction over other claims that are parts of the same case or controversy. *See Chicago v. Int'l Coll. of Surgeons*, 522 U.S. 156, 165-66 (1997) (presence of one claim within federal court's jurisdiction warrants removal of entire case under 28 U.S.C. § 1441(c), including claims not otherwise removable).

This basic principle traces back to *United Mine Workers v. Gibbs*, 383 U.S. 715 (1966), where the Court recognized "that, once a court has original jurisdiction over some claims in the action, it may exercise supplemental jurisdiction over additional claims that are part of the same case or controversy." *Exxon Mobil Corp. v. Allapattah Services*, 125 S. Ct. 2611, 2617 (2005) (describing the holding of *Gibbs*). In particular, *Gibbs* found that, so long as there was a claim before the district court that satisfied the requirements of Article III, the court had the authority to also exercise jurisdiction over additional claims, if "the relationship between [the claims] permits the conclusion that the entire action before the court comprises but one constitutional 'case.'" *Gibbs*, 383 U.S. at 725. The requisite relationship is satisfied if the claims "derive from a common nucleus of operative fact," or if "a plaintiff's claims are such that he would ordinarily be expected to try them all in one judicial proceeding." If so, "there is power in federal courts to hear the whole." *Id.*

While *Gibbs* itself involved the extension of the federal courts' jurisdiction from a claim resting on federal law to a "pendent" claim grounded in state law, several courts have extended its reasoning to cases involving claims which, taken alone, would not have been cognizable due to the absence of standing, rather than the absence of a federal question. For example, in *Sierra Club v. Adams*, 578 F.2d 389, 391-93 (D.C. Cir. 1978), the court concluded that, because plaintiffs had standing to raise a challenge to one aspect of an environmental impact statement, they could also raise a separate claim about another aspect of that statement, despite failing to allege any harm to them related to their second claim. *See also Iowa Indep. Bankers v. Bd. of Governors*, 511 F.2d 1288, 1293-94 (D.C. Cir. 1975).

Wright and Miller describe such cases as deploying a concept of "ancillary standing," under which "[o]nce a genuine case or controversy has been established for standing purposes, nothing in Article III should limit the theories that can be spun out of the 'common nucleus of operative fact.'" 13A WRIGHT & MILLER, *supra*, § 3531.16 at 109 (quoting *Gibbs*); *see also Jackson v. United States*, 881 F.2d 707, 711 (9th Cir. 1989) (invoking concept of "ancillary jurisdiction" to allow the government to litigate an issue for which it did not independently have standing). While Wright and Miller, *supra*, at 110-11, emphasize that the exercise of ancillary standing should be discretionary, taking account of, inter alia, "[e]fficiency and convenience . . . of the courts, parties, and others who are interested in the same issues," they note that taxpayer standing cases may be a particularly appropriate occasion for application of the concept. Indeed, they observe, *id.* at 111 n.14, that this Court appears to have acknowledged such a role for ancillary standing, in *Flast*, 392 U.S. at 104 n.25, in finding that plaintiffs' Establishment Clause standing extended to their Free Exercise claims.[11]

The authority of the district court to extend its jurisdiction from a single claim for which standing is established to other claims that are a part of the same case or

[11] Wright and Miller note that the final sentence of the *Flast* footnote raises doubts about the Court's acknowledgment of such ancillary standing for the Free Exercise claims; however, the most plausible reading of that sentence suggests that it is, instead, a comment on how the Court would analyze the question of Free Exercise Clause standing if considered in isolation from the independent Establishment Clause standing.

controversy also draws support from the text of the supplemental jurisdiction statute, 28 U.S.C. § 1367(a):

> [I]n any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III.

As the Court explained last Term, "Section 1367(a) is a broad grant of supplemental jurisdiction over other claims within the same case or controversy, as long as the action is one in which the district courts would have original jurisdiction." *Exxon*, 125 S. Ct. at 2620. While the primary purpose behind Congress's adoption of § 1367 may have been to clarify the scope of the federal courts' pendent jurisdiction over state law claims, "[n]othing in § 1367 indicates a congressional intent to recognize, preserve, or create some meaningful, substantive distinction between the jurisdictional categories . . . historically labeled pendent and ancillary." *Id.* at 2621. Thus, where the district court has "original jurisdiction over a subset of the claims constituting the action," it has "original jurisdiction of a civil action for purposes of § 1441(a)," and therefore also has supplemental jurisdiction over the remainder of the action. *Id.* at 2623 (citing *Int'l Coll. of Surgeons*, 522 U.S. at 165).[12]

[12] The State Petitioners cite *Lewis v. Casey*, 518 U.S. 343, 357-58 & n.6 (1996), to suggest that standing does not carry over from one claim to another. *See* St. Br. 22. But in *Lewis*, the claims that the plaintiff-prisoners sought to link to their own involved different prisoners facing disparate, and uncertain, obstacles under different circumstances, claims so distinct from plaintiffs' that there was little basis to regard them as part of a single case or controversy. *Cf. City of Los Angeles v. Lyons*, 461 U.S. 95, 106 (1983) (finding standing to challenge past

(Continued on following page)

In the present case, there is little room for question that the two challenged measures – the grants to Daimler of the two tax breaks that comprised the core of the incentives package assembled by State and City to induce Daimler to locate its plant in Toledo – were part of the same transaction or occurrence, and that Respondents' challenges to the two provisions constitute a single Article III case or controversy. *See Raygor v. Regents*, 534 U.S. 533, 540 (2002) (noting Federal Courts Study Committee's use of "same transaction or occurrence" standard in proposing what became § 1367). As the State observes, St. Br. 5-6, both tax incentives were part of a single agreement negotiated among the Petitioners. The counts of Respondents' suit are directed at different components of that single agreement, each of which was alleged to violate the Commerce Clause. If the individual claims of the 10,000 independent dealers in *Exxon* (and likewise the separate claims for non-physical injuries raised by the mother of a physically injured child in the case consolidated with *Exxon*, *see* 125 S. Ct. at 2616) form a single case or controversy, then so must the two claims here, which challenge two Ohio tax provisions applied in a single agreement regarding a single project. *See, e.g.*, *Ammerman v. Sween*, 54 F.3d 423, 424 (7th Cir. 1995) (requiring at least a "loose factual connection between the claims," quoting 13B WRIGHT & MILLER, *supra*, § 3567.1, at 117).

In light of the intimate connection between the counts here, once the district court concluded that it had jurisdiction over some elements of Respondents' suit based on municipal taxpayer standing, *see* J.A. at 78a, it properly extended its jurisdiction to the entirety of the case. All of

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choke-hold incident, but declining to extend standing to completely separate, hypothetical, future incidents).

the "considerations of judicial economy, convenience and fairness to litigants," *Gibbs*, 383 U.S. at 726, favored keeping the entire case in a single forum, and none of the factors identified in § 1367(c) as justifying denial of supplemental jurisdiction were applicable. Indeed, had the court retained jurisdiction over the challenge to the property tax exemption while denying jurisdiction over the challenge to the ITC, the result would have been to compel plaintiffs, who had not sought a federal forum for the case, to litigate these closely connected issues in two separate venues. *See Exxon*, 125 S. Ct. at 2633 (Ginsburg, J., dissenting) (discussing the special importance of supplemental jurisdiction to allow inclusion of claims brought by parties haled into federal court against their will).

C. Under the circumstances of this case, there are no standing barriers that preclude the Court from reaching the merits.

Moreover, the particular context and procedural history of this case provide compelling reasons why the Court should find standing here. Respondents brought this case nearly six years ago in the Ohio state courts, whose standing rules are less restrictive than the federal standards. *See* note 6 *supra*. Due to Petitioners' choice to remove the case, and despite Respondents' efforts to return it to state court, the case has now been extensively litigated in the federal courts, while Daimler has continued to reap the benefits of the challenged tax breaks. In the course of the litigation, Petitioners have repeatedly declined to challenge Respondents' standing, either before the district court, in defending the appeal to the Sixth Circuit, or in their petitions for certiorari here. Nor did either of the courts below raise doubts about their jurisdiction over the case. If this Court were now to deny federal jurisdiction and remand the case to the Ohio courts, all of this effort and time, of both parties and courts, would be for nought, and Respondents would have been compelled to waste six years in a pointless detour beyond their control.

In light of this history, as in *Caterpillar, Inc. v. Lewis*, 519 U.S. 61, 75 (1996), "considerations of finality, efficiency and economy become overwhelming" in disfavoring an outcome that would require the entire case, including the property tax issue on which Petitioners prevailed below, to be relitigated in the state courts. As in *Caterpillar*, the defendants here removed the case, plaintiffs timely objected, and, after the district court declined to remand, several years of litigation in the federal courts brought the case to a decision on the merits. In *Caterpillar*, the Court declined to require all of this work to be done over again in the state courts, even though the district court's assertion of jurisdiction had been in violation of statute, *id.* at 73. In that case, it was the party that had unsuccessfully sought remand and then lost on the merits who subsequently argued for starting over in state court, whereas here, it is the parties who invoked and defended federal jurisdiction who now seek to benefit from an opportunity to litigate the case anew in a different venue. Accordingly, the same "considerations of finality, efficiency and economy" that protected the judgment in *Caterpillar* should also govern here, perhaps even more so where the parties now seeking remand were responsible for bringing the case to federal court in the first place.

Of course, none of these prudential considerations can justify the Court in exercising jurisdiction over the case if it fails to satisfy Article III's requirements of a case or controversy. However, as we now demonstrate, the demands of Article III are met here, and the question of Respondents' standing is prudential, not constitutional, in nature.

First, as discussed in the preceding section, at least one of the challenged elements of the tax break agreement that is the subject of this suit – the property tax exemption – falls within the established parameters for municipal taxpayer standing, thereby ensuring that the case as a whole comes within Article III's ambit. Second, whether or not the Court agrees with Respondents' arguments that their challenge to Ohio's ITC satisfies the requirements for state or municipal taxpayer standing, the ITC, by significantly depleting the revenues in state and local funds to which Respondents contribute through their own taxes, has caused Respondents a real and palpable injury, of precisely the sort that this Court has recognized as satisfying Article III's injury, causation and redressability requirements. In both the Establishment Clause context, *see Flast*, 392 U.S. at 106, and in the municipal taxpayer context, *see Frothingham*, 262 U.S. at 486, the Court has found that the unlawful depletion of tax-supported governmental resources constitutes sufficient injury to affected taxpayers to create an Article III case or controversy.

Aside from instances where there was no showing of any appreciable impact on governmental resources, *see Doremus*, 342 U.S. at 434-35, the reasons the Court has given for withholding federal taxpayer standing have involved the generalized and widely shared nature of the harm, *see, e.g., Frothingham*, 262 U.S. at 487; *Schlesinger v. Reservists Comm. to Stop the War*, 418 U.S. 208, 220 (1974), and the mismatch between the plaintiffs' interests qua taxpayers and the claims they seek to raise, *see, e.g., Valley Forge*, 454 U.S. at 480-81; *Schlesinger*, 418 U.S. at 228. But these considerations relate to factors repeatedly identified by the Court as prudential. *See, e.g., Valley Forge*, 454 U.S. at 474-75 (identifying bar on "generalized grievances, pervasively shared" and the requirement of a claim within the "zone of interests" asserted by plaintiffs as prudential requirements); *Warth v. Seldin*, 422 U.S. 490, 499-501 (1975) (similar, and noting that Art. III's requirements, unlike prudential requirements, can be met even by "an injury shared by a large class of other possible litigants").

While arguments can be made that state taxpayers' claims of injury can be distinguished from those of municipal taxpayers because they are more "generalized" and widely shared, or that Commerce Clause challenges relate differently than Establishment Clause claims to a taxpayer's "zone of interests," such distinctions are matters of degree, not kind, and hence rest on prudential, not constitutional, grounds. *See Fed. Election Comm'n v. Akins*, 524 U.S. 11, 23-24 (1998) (recognizing that generalized grievances can satisfy Article III so long as the harm suffered is concrete). Conversely, any argument that the taxpayers in the present case fail to assert a palpable injury, caused by the allegedly unconstitutional ITC and redressable by its invalidation, would raise identical doubts about Article III standing for taxpayers in familiar municipal and Establishment Clause contexts. *See Flast*, 392 U.S. at 101 (finding no Article III barrier to taxpayer standing); Kristin E. Hickman, *How Did We Get Here Anyway?: Considering the Standing Question in* Daimler-Chrysler v. Cuno, 4 GEO. J.L. & PUB. POL'Y (forthcoming Feb. 2006) (manuscript at 10, *available at* http://ssrn.com/abstract=859784) (noting widespread characterization of *Frothingham* as "implicating only prudential concerns and not Article III standing requirements").

Third, as in *ASARCO*, 490 U.S. at 715-17, there is no doubt that the instant case presents a live case or controversy. In *ASARCO*, like here, the defendants were parties to an agreement with a state, which was challenged by state taxpayers in state court as violating federal law. In *ASARCO*, defendants did not invoke the jurisdiction of the federal courts until they sought review in this Court of an unfavorable final ruling in the state courts. The *ASARCO* Court found that the suit satisfied Article III's requirements, even if plaintiffs failed to qualify for taxpayer standing, where the "parties remain[ed] adverse, and 'valuable legal rights . . . [were] directly affected to a specific and substantial degree by the decision of the question of law,'" and where the suit addressed a specific, concrete agreement rather than seeking a mere advisory opinion. *Id.* at 619 (quoting *Nashville, C. & St. L. R. Co. v. Wallace*, 288 U.S. 249, 262 (1933)). Likewise, the state court suit here involved a dispute about the validity of a concrete agreement that conferred "valuable legal rights" on Daimler that were directly threatened by the litigation brought by taxpayers with interests adverse to it. Admittedly, in the present case, the defendants turned to the federal courts before, not after, their rights had been affected by an adverse state court ruling, but the existence of a case or controversy depends on the concreteness and timeliness of the dispute between the parties and the adverseness of their positions, not on the manner in which federal jurisdiction is invoked. *See Aetna Life Ins. Co. v. Haworth*, 300 U.S. 227, 240-41 (1937).

Once it has been established that Article III's "irreducible constitutional minimum of standing," *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560 (1992), has been satisfied, the decision whether to find standing rests on prudential considerations, which are "essentially matters of judicial self-governance." *Warth*, 422 U.S. at 500. While the courts have identified a number of significant prudential considerations, *see, e.g., Valley Forge*, 454 U.S. at 474-75, these are "merely . . . factor[s] to be balanced" in a prudential calculus, *id.* at 475, not rigid requirements. *See, e.g., Revere v. Mass. Gen. Hosp.*, 463 U.S. 239, 243 (1983) (declining to apply usual prudential factors in light of the prior history of the litigation); *Craig v. Boren*, 429 U.S. 190, 193-94 (1976) (same); *Fraternal Order of Police v. United States*, 173 F.3d 898, 905 (D.C. Cir. 1999).

In the present case, a wide range of considerations of "sound judicial policy," *ASARCO*, 490 U.S. at 613, favor a finding of standing. Of particular significance is the fact that it was defendants, not plaintiffs, who selected and defended the use of a federal forum for a case filed in the Ohio state courts. Had plaintiffs chosen the federal forum, they could hardly complain about the hardship of seeing six years of effort wasted, or accuse defendants of seeking a "second bite of the apple" after losing on the merits. Conversely, where defendants have selected the forum, it is fundamentally unfair for them to now take up the argument that the suit does not belong in federal court.

Consistent with these concerns, the Court has repeatedly focused its analyses of standing on "the party attempting to invoke the federal judicial power." *Id.* at 618; *see also Valley Forge*, 454 U.S. at 477, 478 ("the party who invokes the power") (quoting *Doremus*, 342 U.S. at 434, and *Frothingham*, 262 U.S. at 488). As the district court correctly noted, "the burden of proving jurisdiction, and therefore standing," typically rests on the party removing the case to the federal courts. J.A. at 77a. *See Lujan*, 504 U.S. at 561. Indeed, where the question of standing hinges on prudential, rather than constitutional, considerations, it may be appropriate to treat the issue of prudential standing as waived by defendants who invoke the federal court's jurisdiction by removal, *cf. Lapides v. Bd. of Regents*, 535 U.S. 613 (2002) (finding that state's removal of case to federal court constituted a waiver of Eleventh Amendment immunity), or who fail to raise the issue in the proceedings below. *See Craig*, 429 U.S. at 193 (declining to apply prudential limits on standing where "the lower court already has entertained the relevant constitutional challenge and the parties have sought – or at least have never resisted – an authoritative constitutional determination"); *Board of Natural Res. v. Brown*, 992 F.2d 937, 946 (9th Cir. 1993) ("arguments raising prudential limitations can be deemed waived if not raised in the district court"). To remand the case to the state courts at this point "would be impermissibly to foster repetitive and time-consuming litigation under the guise of caution and prudence." *Craig*, 429 U.S. at 194.

An additional consequence of the absence of an earlier challenge to plaintiffs' standing by either Petitioners or the lower courts is that there has been no opportunity for the standing issues to benefit from the focusing effects of litigation. This Court ordinarily sits as a court of final review, addressing issues only after they have been sharpened and refined by extensive litigation and analysis below. *See, e.g., Adarand Constructors, Inc. v. Mineta*, 534 U.S. 103, 108-09 (2001) (per curiam). In a case like this, where the proceedings below failed to develop complex issues of state and municipal taxpayer standing and supplemental jurisdiction, where the issues do not raise questions of the Court's constitutional jurisdiction, and where the losing party did not object to (and in fact invoked) the federal forum, it may well be the path of wise judicial administration and prudent use of the Court's limited resources to leave further resolution of these thorny issues for another day and uphold Respondents' standing based on the reasons set forth in this section C.

* * *

Should the Court nonetheless conclude that the federal courts lack jurisdiction over the case, the appropriate remedy is a remand of the case to the Ohio state courts. *See* 28 U.S.C. § 1447(c); *Int'l Primate Prot. League v. Adm'rs of Tulane Educ. Fund*, 500 U.S. 72, 89 (1991). Moreover, if there is a remand, Respondents will be entitled to move for attorneys' fees pursuant to § 1447(c). *See Martin v. Franklin Capital Corp.*, 126 S. Ct. 704 (2005).

II. Ohio's Investment Tax Credit violates the Commerce Clause prohibition against state tax measures that discriminate against interstate commerce by providing a direct advantage to in-state economic activity.

A central purpose of the Commerce Clause, and indeed a central motivation behind the framing of the

Constitution, was to create and preserve "a national 'common market,'" *Hunt v. Wash. State Apple Adver. Comm'n*, 432 U.S. 333, 350 (1977), in which economic actors could allocate their activities to the optimal locations without interference from preferential state regulation or taxation. *See Hughes v. Oklahoma*, 441 U.S. 322, 325 (1979) (describing "a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: the conviction that . . . the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation"); *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 328 (1977) ("the very purpose of the Commerce Clause was to create an area of free trade among the several States") (quoting *McLeod v. J.E. Dilworth Co.,* 322 U.S. 327, 330 (1944)). In the oft quoted words of Justice Cardozo, "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." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 523 (1935). Thus, "[i]f there was any one object riding over every other in the adoption of the constitution, it was to keep the commercial intercourse among the States free from all invidious and partial restraints." *Camps Newfound/Owatonna v. Town of Harrison,* 520 U.S. 564, 571 (1997) (quoting *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 231 (1824) (Johnson, J., concurring in judgment)).

Among the primary threats to the functioning of this national common market, both in the Framers' time and today, have been the recurrent efforts of the states to use their tax systems to provide preferential treatment for in-state economic activity. *See, e.g., West Lynn*, 512 U.S. at 193 n.9 ("the Commerce Clause 'grew out of the abuse of the power by the importing States in taxing the non-importing'") (quoting James Madison); *Camps Newfound*, 520 U.S. at 622-23 (Thomas, J., dissenting) (citing examples of interstate tariffs in the post-Revolutionary period); *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 457-58 (1959) (noting that the Court, by 1959, had "handed down some three hundred full-dress opinions" addressing Commerce Clause challenges to state tax measures); *South Central Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999) (invalidating Alabama franchise tax that was calculated more favorably for domestic than out-of-state corporations).

In this long history, the Court's efforts to set appropriate Commerce Clause limits on state taxation have deployed a wide range of different, and at times inconsistent, approaches. Nevertheless, amidst this complexity,

> there emerge . . . some firm peaks of decision which remain unquestioned. Among these is the fundamental principle . . . : No State, consistent with the Commerce Clause, may impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business. The prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause. Permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state businesses would invite a multiplication of preferential trade areas destructive of the free trade which the Clause protects.

Boston Stock, 429 U.S. at 329 (internal quotations and citations omitted).

Over the years, the Court has invoked this rule against discriminatory preferences to strike down a wide array of state tax schemes designed to encourage in-state activity. *See, e.g., Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388 (1984) (invalidating New York corporate income tax credit measured by the share of a company's exporting business conducted from New York); *Fulton Corp. v. Faulkner*, 516

U.S. 325 (1996); *West Lynn*, *supra*. It is this fundamental "anti-discrimination principle," *Maryland v. Louisiana*, 451 U.S. 725, 754 (1981), that Ohio's ITC violates.

A. Ohio's ITC facially discriminates in favor of in-state investment.

Ohio's corporate franchise tax, against which the ITC is applied, is a typical state tax on the apportioned net income of corporations that conduct business in the state. It applies to income earned through the interstate activity of corporations that engage in interstate commerce, so long as they have a taxable presence in Ohio. *See* O.R.C. § 5733.01(B). The tax is calculated by applying the statutory tax rate to the portion of the taxpayer's overall income, wherever earned, that Ohio deems should be attributed to the state based on its three-factor apportionment formula. St. Br. 7. While Ohio's apportionment formula uses the traditional three factors, i.e. the fractions of the taxpayer's property, payroll and sales located in Ohio, *see Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 170 (1983), Ohio assigns the sales factor a weight three times greater than each of the other two factors. St. Br. 7. Due to the triple weighting of the sales factor, how much of a taxpayer's income is taxed in Ohio depends substantially less on where its production activities are located than on where its customers are.

Ohio's ITC, by contrast, applies only to investment in manufacturing machinery and equipment that are placed in service *within the state*. *See* O.R.C. § 5733.33(B)(1) (granting a credit only for investments "installed in this state"). By restricting the credit to in-state activities, while the underlying tax reaches interstate activity, the Ohio statute facially discriminates against interstate commerce.

Consider, for example, the situation of two corporations each subject to Ohio's franchise tax and each making sales of competing goods in Ohio. Assume that, under

Ohio's apportionment formula, each has taxable income in Ohio of $10 million, and therefore would ordinarily be subject to a tax of $850,000. *See* O.R.C. § 5733.06 (statutory rate of 8.5%).[13] Suppose further that one company has its manufacturing facility in Ohio, while the other's is out of state, and that each has recently undertaken a $100 million retooling of its plant. If the Ohio retooling meets the requirements of the Ohio ITC, then the company with the Ohio plant will be entitled to a tax credit of over $1 million in each of the next seven years (i.e. $100 million times 7.5% divided by 7), and therefore will pay no Ohio franchise tax, while its competitor must pay the standard $850,000 annual tax.[14]

As this Court has consistently recognized, "'discrimination' 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." *Oregon Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 99 (1994) (internal quotations omitted). *See West Lynn*, 512 U.S. at 210-11 (Scalia, J., concurring) ("a tax . . . that is nondiscriminatory in its assessment, but that has an 'exemption' or 'credit' for in-state members . . . is no different in principle from [a directly discriminatory tax], and has likewise been held invalid"). This is precisely what Ohio's ITC does. Both the corporation manufacturing its products in Ohio and its out-of-state competitor have identical taxable income subject to Ohio tax. But, because the facially discriminatory ITC makes the actual tax burden on the out-of-state company far higher, the in-state company is placed at "a direct commercial advantage," *Boston*

[13] Because the first $50,000 of apportioned corporate income is subject to a lower tax rate, the actual amount would be slightly less.

[14] This Court found a similar simple example, offered by the United States, to be helpful to its analysis in *Maryland v. Louisiana*, 451 U.S. at 757 n.28.

Stock, 429 U.S. at 329, with respect to its out-of-state competitor. It is this blatantly discriminatory design of ITCs, like Ohio's, that has led commentators to discuss such provisions as paradigmatic examples of tax breaks that violate the Commerce Clause. *See, e.g.*, Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 817-18 (1996); Robert D. Plattner, *State Business Tax Incentives: Are They Vulnerable to Constitutional Attack*, 2000 ST. TAX TODAY 128-19 (July 3, 2000).

Like many of the discriminatory tax provisions that have previously been found unconstitutional, Ohio's ITC has the purpose and effect, not only of treating in-state businesses more favorably than their interstate competitors, but also of encouraging corporations to locate new economic activity inside Ohio, rather than elsewhere. *See, e.g., Fulton*, 516 U.S. at 333 & n.3; *Maryland v. Louisiana*, 451 U.S. at 756-57; *Halliburton Oil Well Cementing Co. v. Reilly*, 373 U.S. 64, 72 (1963). As the Court of Appeals explained, in describing how the provision discriminates against interstate activity:

> as between two businesses, otherwise similarly situated and each subject to Ohio taxation, the business that chooses to expand its local presence will enjoy a reduced tax burden, based directly on its new in-state investment, while a competitor that invests out-of-state will face a comparatively higher tax burden because it will be ineligible for any credit against its Ohio tax.

Pet. App. at 6a.

Petitioners argue that because the credit's benefits are available to any corporation that chooses to locate new economic activity in Ohio, it does not discriminate against out-of-state businesses. St. Br. 41-42; Br. for Pet'r DaimlerChrysler ("DC Br.") 45. But, as in *Bacchus Imps. Ltd. v. Dias*, 468 U.S. 263 (1984); *Westinghouse*, *supra*; and *Boston Stock*, *supra*, the fact that Ohio's ITC does not discriminate on the basis of a company's domicile or the location of its *pre*-investment activity does nothing to ameliorate the ITC's facial discrimination on the basis of where the company sites its new investments (and where it is located *post*-investment, i.e., at the time that it enjoys the preferential treatment).

Petitioners also argue that the ITC's differential treatment of similarly situated companies does not constitute discrimination, because, as a result of their different choices about where to locate, the two businesses are no longer "similarly situated." St. Br. 47-48; DC Br. 40-42. In support, they note that one effect of locating a plant out-of-state will be to reduce the proportion of the business's income that is apportioned to Ohio and subject to tax there, while an in-state siting will have the opposite effect. Thus, Petitioners suggest, a business choosing an out-of-state location will see its Ohio tax reduced, while one locating in-state will see its tax increased. They argue that, under these circumstances, the ITC only serves to counterbalance the extra tax burden imposed on the business choosing the in-state location.

In *Westinghouse*, however, the Court directly rejected precisely this argument. *See* 466 U.S. at 400-02 n.9. There, the Court began with a simple example of the discriminatory effects of the challenged credits, in which three hypothetical businesses with identical apportionment ratios had different levels of export activity located in New York and therefore earned different sizes of credits, with the result that the business with the greatest export activity in New York paid the least tax. But the Court went on to observe that this example overlooks the fact that the shifting of more export activity into New York would also result in an increase in the share of the business's income apportioned to New York and, hence, an increase in its New York tax, an increase that is only partially offset by the increased export credit.

However, rather than taking this difference as a justification for the alleged discrimination, as Petitioners here urge, the Court turned instead to a more refined analysis, which examined the effect of the credit on the effective tax rates paid by the different businesses on their income apportioned to New York. While the absolute tax liability was greatest for the business with the most export activity in New York, that business also, due to the credit, paid the lowest effective tax rate, thus evidencing, in the Court's analysis, the credit's discriminatory treatment which violated the Commerce Clause.

Applying the *Westinghouse* approach to this case, a business which locates its new plant outside of Ohio will face an effective tax rate of 8.5% on its income apportioned to Ohio, since it earns no ITC. By contrast, its competitor which chooses an Ohio location for its new facility will, for the next seven to ten years, pay an effective tax rate of less than 8.5% due to the reduction of its tax by the ITC. Just like in *Westinghouse*, the location based credit scheme here discriminates in favor of in-state activity by affording a lower effective tax burden to businesses locating their activities in the state. In fact, the discrimination caused by the Ohio ITC will typically be more dramatic and blatant than the discrimination noted in the *Westinghouse* examples, because, due largely to Ohio's triple weighting of the sales component of its apportionment formula (a factor largely unaffected by the location of production facilities), the reductions in a business's Ohio tax liability due to location of a new plant outside the state will typically be dwarfed by the tax reductions achieved by its in-state competitor who qualifies for the ITC.[15]

[15] To see why the tax reduction from locating new facilities out of state will typically be far smaller than the benefits of the ITC for a competitor locating in Ohio, consider the detailed, realistic example set forth in the App. to Br. of Amicus Curiae Center on Budget and Policy Priorities. There, the company locating its new facility in "Other State"

(Continued on following page)

In any case, Ohio's rules for the apportionment of income reflect its judgments about how to fairly determine the share of a business's income that is earned in, and should be subject to tax in, Ohio. To the extent that location of a new facility outside the state reduces a business's Ohio franchise tax, that reduction simply reflects Ohio's recognition that the location of productive capacity is a relevant factor in determining where income is earned.

With its discriminatory ITC, Ohio has overridden its fair apportionment system by taxing those businesses which locate their manufacturing capacity out of state at the statutory tax rate, while imposing substantially lower effective tax rates on those businesses whose productive capacity is located within Ohio's borders. The result is a direct competitive advantage for the in-state businesses, which, just like a tariff, offers economic benefits not only to the in-state businesses but to their local suppliers and employees, and, also just like a tariff, benefits the local economy by encouraging additional businesses to locate their activities in-state to avoid the burdens of differentially heavier taxation. *See, e.g., West Lynn*, 512 U.S. at 193 (describing the harmful effects of tariffs).

The prospect of achieving these local benefits makes ITCs and similar location-based tax breaks extremely attractive to state policymakers, and it is perhaps unsurprising that the vast majority of states have adopted ITCs and similar measures. *See* St. Pet. 22 n.5. But, to the extent that one state is helped by such measures, it is at the expense of other states, and at the expense of interstate friction and disruption of the efficient allocation of resources in an open national common market. *See, e.g.,*

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thereby reduced its Ohio tax liability by only $17,000, while the otherwise identical company locating its facility in Ohio earned an ITC of more than $96,000 for each of the next seven years, more than enough to eliminate its entire Ohio tax liability. Similar outcomes will result from a very wide range of plausible scenarios.

KENNETH THOMAS, COMPETING FOR CAPITAL 1-49 (2000); Br. of Amici Curiae Econ. & Pub. Policy Professors Randy Albelda, et al. These are precisely the ills of "economic Balkanization," *Hughes v. Oklahoma*, 441 U.S. at 325, against which the Commerce Clause was directed, with its central premise that "the peoples of the several states must sink or swim together, and that in the long run prosperity and salvation are in union not division." *Baldwin*, 294 U.S. at 523.

Petitioners argue that the effect of Ohio's ITC is actually to encourage and reward interstate investment in Ohio by out-of-state businesses, and that the credit thereby supports Commerce Clause goals of furthering interstate commerce. St. Br. 49; DC Br. 44. But,

> [a] State may no more use discriminatory taxes to assure that nonresidents direct their commerce to businesses within the State than to assure that residents trade only in intrastate commerce. . . . [The Commerce Clause's] free trade purpose is not confined to the freedom to trade with only one State; it is a freedom to trade with any State, to engage in commerce across all state boundaries.

Boston Stock, 429 U.S. at 334-335.

Similarly, Petitioners and their amici attempt to defend states' use of ITCs and similar devices on the ground that they are important tools in enhancing the United States' position in the global competition for business investment and jobs. *See, e.g.,* St. Br. 4, 50; Br. of Amici Curiae Nat'l Governors Ass'n et al. 1. However, leaving aside the lack of any evidence that state tax breaks have the capacity – or were intended – to influence international investment choices, the prospect of the fifty states using their tax regimes to shape the nation's international trade policy runs directly counter to the Constitution's delegation of authority over foreign trade to Congress. *See, e.g., Kraft Gen. Foods v. Iowa Dep't of Rev.*

& Fin., 505 U.S. 71, 82 (1992) (invalidating state tax measure that discriminated against foreign commerce). Such Foreign Commerce Clause concerns are particularly strong when a state's actions prevent the nation from "speaking with one voice" in regulating international trade relations, *see, e.g., Japan Line, Ltd. v. Los Angeles County*, 441 U.S. 434, 451 (1979), by raising conflicts with national policies embodied in treaty commitments. This is precisely what tax breaks like Ohio's ITC threaten to do. *See, e.g.,* Request for the Establishment of a Panel by the European Communities, *United States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS317/2 (June 3, 2005) (World Trade Organization challenge to location-based tax breaks offered by states to Boeing); *see also* Arthur Rogers, *EC Will Investigate Kansas Tax Breaks Aimed at Luring British Production Plant*, BNA DAILY TAX REPORT, April 15, 2005 (describing potential for a similar challenge).

> While the Federal Government may seek to increase domestic employment and improve our balance-of-payments by offering tax advantages to those who produce in the United States rather than abroad, a State may not encourage the development of local industry by means of taxing measures that invite a multiplication of preferential trade areas within the United States, in contravention of the Commerce Clause.

Westinghouse, 466 U.S. at 405 (internal quotations and citations omitted).

B. Petitioners' attempts to narrow the antidiscrimination principle are incompatible with precedent and the Commerce Clause's central purposes.

Petitioners face a daunting challenge. They cannot dispute that the purpose and effect of Ohio's ITC is to grant to businesses that locate new investment in Ohio distinctively favorable treatment not available to competitors who locate comparable new investment elsewhere. And yet, they are unable to point to a single case in which the Court has upheld a measure that provided preferential tax treatment conditioned upon in-state economic activity.

Petitioners seek to avoid the conclusion that this "direct commercial advantage," *Boston Stock*, 429 U.S. at 329, for in-state business activity violates the Commerce Clause's anti-discrimination principle by proposing several novel and narrow interpretations of the Court's anti-discrimination case law, which, they contend, allow for a distinction between the measures previously invalidated by the Court and Ohio's ITC. These interpretations seek to restrict application of the anti-discrimination principle to measures that impose penalties on out-of-state activity, rather than benefitting in-state activity.

In fact, however, Petitioners' novel interpretations not only fail to accommodate the cases or the Court's explanations, but they would also have the effect of largely eviscerating the Commerce Clause's bar against discriminatory tax measures, by re-introducing formalistic distinctions easily manipulated by state policymakers wishing to revive forbidden discriminatory schemes. And their reinterpretations of the anti-discrimination principle are not needed – as Petitioners suggest they are – to preserve the states' broad autonomy over their tax policies and other measures to support their local economies. To avoid severe damage to a long-standing, straightforward and effective element of its Commerce Clause jurisprudence, the Court should reject these unwarranted proposals for ad hoc change.

i. Petitioners' proposed narrowing of the anti-discrimination principle to distinguish between tax benefits and tax penalties should be rejected.

Petitioners' primary argument is that the Commerce Clause only invalidates state tax measures as discriminatory if they either function as tariffs levied directly on interstate transactions or impose tax penalties on businesses for their out-of-state activities. They contend that Ohio's ITC, since it applies against an income tax, rather than a transactional tax, and since it provides tax reductions ("benefits") for in-state activity, rather than tax increases ("penalties") for out-of-state activity, does not run afoul of either prong of this restrictive framing of an anti-discrimination principle. *See* St. Br. 35-41; DC Br. 26-30.

This bifurcated categorization of the case law had its origins in a law review article written to contain the implications of the Court's rapidly expanding body of anti-discrimination tax cases, and particularly *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984). *See* Philip Tatarowicz & Rebecca Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 VAND. L. REV. 879 (1986). But this attempted compartmentalization of the Court's anti-discrimination jurisprudence can account neither for the Court's explanations of its reasoning nor for a number of its decisions. *See* Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 813-15.

Petitioners' proposed framework depends on a crucial distinction between provisions that increase taxpayers' burdens due to out-of-state activity and those that "merely" diminish burdens on account of in-state activity. But they are unable to cite a single case in which the Court has deployed such a distinction. On the contrary, the Court has expressly, and quite sensibly, disavowed any distinction, for anti-discrimination purposes, between tax benefits and burdens:

> Virtually every discriminatory statute allocates benefits or burdens unequally; each can be viewed as conferring a benefit on one party and a detriment on the other, in either an absolute or relative sense. The determination of constitutionality does not depend upon whether one focuses upon the benefited or the burdened party.

Bacchus, 468 U.S. at 273. *See Westinghouse*, 466 U.S. at 404 ("Nor is it relevant that New York discriminates . . . by disallowing a tax credit rather than by imposing a higher tax. The discriminatory economic effect of these two measures would be identical.").

Petitioners seek to deploy their analytic schema to limit the impact of the Court's holding in *Westinghouse*, *supra*, which found unconstitutional New York's corporate income tax credits that were measured by the extent of the taxpayer's in-state export activities. The *Westinghouse* Court did observe that the scheme invalidated there, not only increased the credits as activity in New York increased, but also decreased the credits as activity elsewhere expanded, a feature that the Court described as the credit's "most pernicious feature." *Id.*, 466 U.S. at 401 n.9. But a thorough reading of the Court's opinion makes clear that this feature of the New York provision was not, as Petitioners insist, essential to the Court's ruling. In fact, the Court focused primarily on the benefits provided for New York activity, describing the provision as "an attempt to 'provide a positive incentive for increased business activity in New York.'" *Id.* at 393. And when the Court offered three detailed examples of the workings of the credit, each intended to show the discriminatory effects of the provision, only the last one exemplified the "penalty" effect, while the others focused on the benefits that result from increasing in-state activity. *Id.* at 401 n.9. As prominent scholars have observed, "The clear thrust of the opinion was that any provision that reduces the taxpayer's 'effective [in-state] tax rate' as the taxpayer engages in more in-state activity violates the Commerce Clause." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 815 (citations omitted).

Nor can their categorization accommodate a number of the Court's other anti-discrimination decisions. For example, in *Maryland v. Louisiana*, *supra*, the Court struck down several aspects of Louisiana's tax on the transportation in Louisiana of off-shore natural gas, including a credit allowing taxpayers to use the tax on off-shore gas to reduce severance taxes on (unrelated) in-state mineral extraction.[16] As the Court explained, the discriminatory feature of this provision was not any penalty imposed on out-of-state operations, but rather the benefit it provided for in-state activity and the resultant incentive "to invest in mineral exploration and development within Louisiana rather than to invest . . . in other States." *Id.* at 757. Other examples that cannot be accommodated within Petitioners' framework include *American Trucking Ass'n, Inc. v. Scheiner*, 483 U.S. 266 (1987) (striking down Pennsylvania's flat-rate axle tax because it favors businesses using their trucks exclusively in-state) and *Camps Newfound*, *supra* (invalidating a Maine property tax exemption restricted to charitable organizations providing services primarily to in-state residents). The simple fact is that the Court's consistent approach has been to invalidate measures that are structured to favor in-state over out-of-state activity, without regard to whether the discrimination is achieved by providing a benefit for in-state activity or imposing a burden on out-of-state alternatives.

Were the Court to change course and adopt the narrowed anti-discrimination analysis suggested by Petitioners, it would do serious harm to the efficacy and clarity of this element of Commerce Clause jurisprudence. The

[16] Petitioners suggest that *Maryland v. Louisiana* is a case that fits within their narrow categories, *see* St. Br. 39; DC Br. 28, but they do so by limiting their discussion to a second element of the Louisiana tax scheme, its exemptions for gas used for specified in-state activities, which the Court also struck down. They simply omit any discussion of the Court's invalidation of the credit provision, which cannot be forced into their artificial framework.

Court's present test, whether there is "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter," *Oregon Waste*, 511 U.S. at 99, focuses effectively and straightforwardly on the "practical effect," *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), of the challenged measure. By contrast, the proposed distinction between benefits for in-state activity and penalties on out-of-state activity would reintroduce precisely the focus on formal phrasing and technical structure that bedeviled the Court's pre-*Complete Auto* case law. *See West Lynn*, 512 U.S. at 201 ("our cases have eschewed formalism for a sensitive, case-by-case analysis of purposes and effects"). If the Court were to adopt Petitioners' distinction, the states could, with ingenuity, revive many of the discriminatory schemes struck down by the Court in new guises that used "benefits" instead of "burdens" to achieve identical practical effects.[17] It is precisely to avoid such a triumph of form over substance that the Court has emphasized the futility of a distinction between benefits to one class of taxpayers and burdens on another in assessing the discriminatory character of taxes affecting interstate activity. *See, e.g., Bacchus*, 468 U.S. at 273; *cf. West Lynn*, 512 U.S. at 211 (Scalia, J., concurring) (arguing that a credit against a neutral tax is "no different in principle" from a directly discriminatory tax and must be treated comparably).

[17] For example, forbidden exemptions from excise taxes, like those in *Bacchus*, *supra*, or *New Energy Co. v. Limbach*, 486 U.S. 269 (1988), could be recast as identically measured credits against a corporate income tax. And the credit scheme struck down in *Westinghouse* could be recast to avoid its "penalty" feature by calculating it on the basis of the dollar volume of in-state export activity, rather than using the problematic ratio of in-state to total export activity.?? [18] While new

ii. The suggestion that the Commerce Clause is inapplicable here because there is no regulation of interstate commerce flies in the face of both precedent and logic.

For the first time in its brief here, Daimler introduces a new and far more radical variant of the proposal to draw a sharp distinction between tax benefits and burdens. DC Br. 32-40. It asserts that the challenged Ohio tax scheme does not impose any burden on interstate commerce and hence does not come within the scope of Commerce Clause constraints at all, because a state tax "triggers dormant Commerce Clause scrutiny only when it imposes a burden on interstate commerce." *Id.* at 34. Thus, Daimler suggests, the measure challenged here, since it merely provides a benefit for in-state activity, does not "regulate" interstate commerce at all, and hence cannot "transgress the dormant Commerce Clause's limitations." *Id.* at 33.

This argument rests on the premise that it is "a prerequisite for discrimination analysis under the dormant Commerce Clause" that "the underlying state tax burdens interstate commerce." *Id.* at 34. To the extent that Petitioner contends that "the underlying state tax" here, Ohio's corporate franchise tax, does not burden interstate commerce, the simple answer is that, as a tax on an apportioned share of the total income earned by corporations through the operation of an interstate business, the franchise tax is unquestionably a tax upon, and thereby a burden upon, interstate commerce. This Court's voluminous case law discussing Commerce Clause limitations on state taxes on apportioned corporate income give ample witness to that fact. *See, e.g., Container Corp.*, *supra*; *Northwestern States*, *supra*.

At times, Petitioner appears to be making a somewhat narrower argument – that the Court has only found tax breaks unconstitutional "where the underlying state tax reached – and as a result burdened – interstate transactions against which the state's tax exemption or credit supposedly discriminated." DC Br. 37. The argument is apparently that, since Ohio's franchise tax "does not apply to out-of-state capital investments," *id.* at 36, Ohio's ITC cannot violate the Commerce Clause by "supposedly" discriminating against such investments.

Of course, the reason that Ohio's franchise tax "does not apply" to out-of-state investment is because it is not a tax on investments at all, but rather a tax on the income that may be earned from such investments.[18] And Daimler is able to point to absolutely nothing in case law or in scholarly commentary to support its suggestion that the Commerce Clause only applies when such a narrow condition is met. Indeed, many of the tax breaks struck down by this Court as discriminatory involved taxes that "did not apply" to the kinds of transactions that qualified for (or were discriminated against by) the challenged tax breaks. For example, in *Camps Newfound*, *supra*, the Court struck down an exemption from Maine's property taxes that was conditioned on the exempted property being used to provide charitable services primarily to in-state residents, but the property tax certainly did not "apply to" or "reach" the provision of services to out-of-state residents, because it was a tax on property not on services. *See also, e.g., Maryland v. Louisiana*, *supra* (invalidating a credit against in-state severance tax based on interstate tax on transportation of off-shore gas); *Fulton*, *supra* (invalidating a reduction in a property tax

[18] While new out-of-state investment may, as Daimler notes, DC Br. 35-36, reduce the share of the company's total income that is apportioned to Ohio, a substantial proportion of the income earned through that new investment is still likely to be apportioned to Ohio, especially in light of the triple weighting that Ohio assigns to the sales factor.

on owners of shares of stock based on how much of the issuer's business was conducted in-state).

As these examples underscore, and contrary to Daimler's assertion, DC Br. 39, this Court has repeatedly and appropriately invalidated state tax breaks notwithstanding the fact that "the tax did not . . . levy against interstate transactions alleged to be prejudiced." And here, again, were the Court to adopt Petitioner's proposed narrowing of the Commerce Clause's reach, it would essentially be inviting the states to structure an endless array of blatantly discriminatory tax breaks as credits against state taxes that were not themselves levied on the kind of activity being discriminatorily rewarded. *See Westinghouse*, 466 U.S. at 404 (rejecting the possibility of a state using credits against a franchise tax on income to accomplish what would be forbidden for a parallel location-based reduction in a transactional tax). The result would be precisely the triumph of form over function that the Court emphatically rejected in *Complete Auto*, 430 U.S. at 288 (renouncing reliance on "formalism [that] merely obscures the question whether the tax produces a forbidden effect"); *see West Lynn*, 512 U.S. at 201.

iii. The anti-discrimination principle leaves intact a wide range of state measures to promote economic growth and does not invite judicial intrusion into state tax policy-making.

Petitioners suggest that an anti-discrimination principle broad enough to invalidate Ohio's ITC will inevitably carry the Court's dormant Commerce Clause jurisprudence far beyond its familiar boundaries, and that their narrowed reinterpretations are necessary to keep the Clause within reasonable bounds. In particular, they contend both that an unrestricted anti-discrimination principle would invalidate virtually any state efforts to promote development of their local economies, DC Br. 37; St. Br. 45-46, and that it would require the Court to impose a totally uniform system of taxation on the states, St. Br. 45-47; DC Br. 47-48.

These fears, however, are entirely groundless. There are a great many ways that the states are free to shape their tax systems to create a favorable environment for economic activity, which do not involve any kind of preferential treatment for in-state activity. They can reduce the rates at which they tax business income; they can exempt business property (or specified types of business property) from property taxation, or tax it at lower rates than other kinds of property; they can exempt business inputs from sales taxation. In each case, such measures reduce the tax burdens on in-state businesses, but do so without favoring in-state businesses over out-of-state competitors (which in some cases, e.g. property taxation, are not subject to tax at all, and in others, e.g. lowered income tax rates, are treated identically to their in-state rivals).

If the Court is to fulfill the Commerce Clause's function of protecting the national economy and the states themselves from the "Balkanization" that results from protectionist preferential tax treatment of in-state economic activity while preserving the states' broad autonomy over matters of tax and economic policy, it is essential to draw as bright a line as possible on the continuum between tariffs and simple variations in tax rates and tax bases. *See West Lynn*, 512 U.S. at 211-12 (Scalia, J., concurring) (seeking to draw "a clear, rational line"). In the long evolution of the Court's dormant Commerce Clause jurisprudence, the anti-discrimination principle has remained a "firm peak[ ] of decision," *Boston Stock*, 429 U.S. at 329, because it provides a clear boundary which leaves wide latitude to the states in matters of taxation, while barring "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." *Oregon Waste*, 511 U.S. at 99.

Beyond taxation, the Commerce Clause also leaves wide latitude for state programs in support of economic development, ranging from worker training and infrastructure construction to low interest loans and preferential purchases of in-state goods or services. As the Court has repeatedly recognized, such state programs, involving the deployment of state resources, are not, ordinarily, "the kind of action with which the Commerce Clause is concerned," *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 805 (1976), because "the Commerce Clause responds principally to state taxes and regulatory measures impeding free private trade in the national marketplace." *Reeves, Inc. v. Stake*, 447 U.S. 429, 436-37 (1980). Where a state uses its own resources to "enter[ ] into the market itself," its conduct does not trigger Commerce Clause scrutiny, even if it participates in the market in a manner that favors in-state activities or actors. *Alexandria Scrap*, 426 U.S. at 806; *cf. New Energy*, 486 U.S. at 277 (distinguishing tax measures from direct spending programs because taxation is "a primeval governmental activity").

Of course, as Petitioners observe, DC Br. 33, the states may well be able, through such direct uses of state resources, to provide incentives for businesses that, from the businesses' perspective, are quite similar to an ITC or other tax incentives barred by the Commerce Clause. But here, again, the Court's boundary makes good sense. Not only does it draw a bright line which is solidly grounded in the Commerce Clause's focus on the power to "regulate Commerce . . . among the several States," U.S. Const. art. I, § 8, cl. 3, but it also reflects the important practical differences, from the perspective of state policymakers, between the relative ease with which tax breaks can be enacted and the difficulty and complexity of enacting expenditure programs, and hence the need for stricter external constraints on the former. *See, e.g.,* Dan T. Coenen, *Untangling the Market-Participant Exemption to the Dormant Commerce Clause*, 88 MICH. L. REV. 395, 480-81 (1989).

Thus, the prohibition on tax measures that discriminate against interstate commerce leaves ample opportunity for the states to foster local economic development, both through tax policies and through other governmental programs. As the Court has stated over and over again in cases striking down discriminatory state tax provisions, nothing in those decisions "prevent[s] the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry," *Boston Stock*, 429 U.S. at 336, or from "enact[ing] laws pursuant to [their] police powers that have the purpose and effect of encouraging domestic industry," *Bacchus*, 468 U.S. at 271. The restriction imposed by the Commerce Clause is directed not at ends, but at means. The Court has consistently been careful to distinguish the legitimacy of the state's purposes from the acceptability of the means selected to further them, *see id.*, and to clarify that the permissible means do not include measures that discriminate between in-state and out-of-state activity, *see, e.g., Boston Stock*, 429 U.S. at 337. The specific sorts of state competition for industry that the Court's dicta have countenanced, such as uniformly applicable reductions of state taxes and government support for services needed by business, *see, e.g., West Lynn*, 512 U.S. at 199 n.15, include only provisions that do not differentiate benefits or burdens based on a business's location.

Ohio's ITC, by contrast, expressly provides a direct commercial advantage to businesses making their new investments within the state, by subjecting them to a lower tax burden than their competitors who locate new investments elsewhere. This is precisely the kind of discrimination that this Court has consistently invalidated, in furtherance of "the dormant Commerce Clause's fundamental objective of preserving a national market for competition undisturbed by preferential advantages conferred by a State upon its residents or resident competitors," *Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 299 (1997).

CONCLUSION

For these reasons, the Court should find that the federal courts have jurisdiction over this case and should affirm the Sixth Circuit's decision finding Ohio's investment tax credit in violation of the Commerce Clause. Should the Court conclude that the federal courts lack jurisdiction, the appropriate remedy is a remand to the Ohio state courts, from which it was removed.

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