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Commerce Clause Constraints on State Business Location Incentives

Peter D. Enrich

Over the past several decades, states and municipalities in the United States have engaged in an accelerating competition to reward business location and investment through the use of a wide range of financial incentives, notwithstanding overwhelming evidence of the minimal efficacy and the high costs of such incentives. This interstate competition for economic activity is reminiscent of the eighteenth-century tariff wars among the states that were a primary impetus behind the crafting of the U.S. Constitution and its assignment of responsibility for the regulation of interstate commerce to the federal government. Over the ensuing centuries, the courts have consistently applied the Constitution's Commerce Clause to constrain parochial state measures that interfered with the free flow of commerce in a national common market.

This article considers whether, and to what extent, the Commerce Clause limits the ability of states and localities to engage in the incentive competition that has proliferated in recent decades. In particular, I argue that well-established Commerce Clause principles forbid a wide range of the location-based tax incentives that states and localities offer to businesses. At the same time, it is important to recognize that judicial application of the Commerce Clause offers, at best, a blunt instrument for addressing the challenges of interstate competition for business investment. This article will also canvass a range of limitations and shortcomings of this constitutional constraint on governmental efforts to intervene in business location decisions.

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I. The Context: Interstate Competition for Business Investment

By the late 1990s, virtually every state, and a great many localities, was aggressively engaged in offering a wide range of incentives for businesses that located their investment and employment in the jurisdiction.[1] While the array of incentives offered by the states often includes expenditures of governmental funds (e.g., for infrastructure improvements, worker training, or, in some cases, cash grants or low-cost loans) or regulatory accommodations, the primary focus of governmental intervention has been through a broad palette of tax incentives. Investment tax credits, job creation credits, and property tax abatement programs have become virtually universal, and in recent years more and more states have been adjusting their rules for the apportionment of corporate income to focus primarily, if not exclusively, on the location of sales, rather than of payroll and property.

Some of these tax incentives are designed as discretionary programs whose benefits are awarded by negotiation between businesses and state officials; others are specifically crafted and enacted to respond to particular industries or even to particular businesses; while still others are structured as entitlements that can be utilized by any company that satisfies their broad criteria. Most states offer long lists of different types of tax incentives geared toward different business situations, and scarcely a week goes by without reports of at least one state proposing or enacting a new tax incentive program. Indeed, a whole business has emerged of consultants who help businesses to keep track of the available incentives and to ensure that they claim all of the incentives to which they are entitled. Reports of incentive packages measuring in the hundreds of millions of dollars have become increasingly frequent, and it is not uncommon for the incentive package for a large plant to be big enough to excuse the company from any state or local tax liability in the jurisdiction for a period of years.

Putting a price tag on all of this activity is not easy. But one careful scholarly effort, extrapolating from the few states providing solid data, estimated that the total cost of state and local incentives, both tax and non-tax, in 1996 approximated US$50 billion.[2] The number a decade later is surely substantially larger and represents a significant fraction of state and local revenues.[3] Perhaps equal-

1 Under U.S. constitutional principles, local governments are political subdivisions of the states, and local actions are, in general, subject to the same constitutional constraints as state actions. So, in this article, I will not distinguish between state and local measures, and will generally use the term "state" as shorthand for "state and local."

2 *See* Kenneth Thomas, Competing for Capital – Europe and North America in a Global Era 158-59 (2000).

3 For the sake of comparison, total state and local own-source revenues in 1995-96 were US$988 billion. U.S. Census Bureau, U.S. State and Local Government Finances by Level of Government: 1995-96, *available at* http://www.census.gov/govs/estimate/9600us.html.

ly importantly, the proliferation of corporate tax breaks is one of several factors that have contributed to a dramatic shift in the distribution of state and local tax burdens between businesses and individual taxpayers. Between 1979 and 1999, businesses' share of total state income tax revenues declined from 29 percent to 15 percent, and the business share of local property tax revenues has likewise dropped sharply.[4]

Despite these high costs, state and local tax incentives do not appear to exert a significant influence on the location of business activity. As business tax incentives have proliferated, so have econometric analyses of the effects of state and local tax burdens and specifically of state and local tax breaks on business activity and investment. Recent surveys of the dozens of empirical studies conclude that state and local tax breaks have been shown to have, at best, only marginal effects on business location.[5]

Several factors contribute to this somewhat surprising conclusion. First, state and local taxes are generally too small to be a major factor in the economics of business location decisions. For the typical business, state and local taxes represent only 1.2 percent of the cost of doing business in the United States.[6] So, even an incentive package that completely eliminates a company's tax obligation will only have a modest effect on overall costs. Variations in other factors, such as costs and skills of labor, access to resources and markets, and utility costs, are likely to overwhelm any small potential savings from tax reductions. Second, since all U.S. jurisdictions are offering a wide array of tax breaks, the potential savings from one state's incentives will be largely offset by those available from competing locations. Moreover, even the modest positive effects of lower taxes on business location found in the research assume that all other factors, including levels of state and local government spending, are held constant. But, in fact, states, unlike the federal government, are subject to balanced-budget requirements, and the evidence reveals robust positive relationships between spending on public services and economic activity.[7] So, if tax breaks reduce the funding available for services, any positive effects of reduced taxes are liable to be offset by the negative effects of reduced services.

4 Robert Tomsho, *In Toledo, a Tension between School Funds and Business Breaks*, Wall St. J., July 18, 2001, at A1 (reporting U.S. Census data). *See* also Laird Graeser & Al Maury, *Business Taxes – Quo Vadimus*, 7 St. Tax Notes 917, 918 (1994) (summarizing data reported by the U.S. Advisory Commission on Intergovernmental Relations indicating that state business taxes had declined from 50 percent of state taxes in the 1950s to 25 percent by 1990).

5 *See* Robert G. Lynch, Rethinking Growth Strategies – How State and Local Taxes and Services Affect Economic Development (2004); Alan Peters & Peter Fisher, *The Failures of Economic Development Incentives*, 70 J. Amer. Planning Assoc. 27 (Winter 2004).

6 *See* Lynch, *supra* n. 4, at 4.

7 *See id.* at 43-46.

Even if a state's location incentives do have some positive effect on business investment in that state, the effect of the incentive competition from a national perspective is at best a zero-sum game. Despite occasional suggestions by defenders of state and local incentives that they might help the United States compete in the international market for investment, there is no credible evidence that these incentives are of a scale to have such effects, nor that they were ever designed with such a purpose in mind. At best, these incentives affect the location of economic activity among the states, not its overall level. Indeed, to the modest extent that state incentives are effective and influence businesses to site their activities at locations that would otherwise be economically disfavored, the incentives are likely to reduce, rather than enhance, national economic efficiency.[8] Thus, the primary effect of the states' incentive competition, from a national perspective, is not to encourage or expand economic activity, but rather to lower the general level of state and local taxation of businesses, in a "race to the bottom" that either shifts tax burdens to other taxpayers or reduces the resources available for state and local governmental services.

Notwithstanding the evidence of the minimal efficacy, and deleterious effects, of state tax incentive proliferation, state policymakers have shown little inclination to walk away from the competition. As many analysts have observed, the states are caught in a version of a prisoners' dilemma, where it is irrational for any one state to stop offering incentives while other states remain free to continue providing them.[9] Indeed, even to the extent that state officials recognize the virtual irrelevance of incentives to business location decisions, they are reluctant to forego the use of a tool which, regardless of its actual effect on business behavior, is a powerful way to communicate to voters their commitment to the state's economic vitality. Absent some external constraint, the competition among states and localities to offer ever-larger incentive packages appears unlikely to abate.

II. The Legal Framework: The Commerce Clause's Role

Most U.S. lawyers will be quite surprised to find a discussion of these issues in a journal devoted to competition policy. Unlike the EC framework, within which the problem of state aid is conceptualized as one among many forms of interference with the functioning of competitive market forces, U.S. antitrust law focuses almost exclusively on anticompetitive activities of private actors. Indeed, the presence of state action ordinarily suffices to immunize conduct, even by private

8 For a description and critique of an argument that state incentives might actually help to optimize the efficiency of business location decisions, *see* Peter D. Enrich, *Business Tax Incentives: A Status Report*, 34 Urb. Lawyer 415, 418-22 (2002).

9 *See, e.g.,* Thomas, *supra* n. 2, at 33-40.

parties, from antitrust scrutiny.[10] The notion that state or local use of incentives to reward local business activity might raise antitrust concerns would find no toehold in U.S. law.

Instead, the U.S. legal system's limitations on state interference with an open national common market are conceptualized as aspects of the constitutional framework of federalism, which establishes the respective scope and limits of national and state authority, a body of law that arose more than a century before the emergence of antitrust law's constraints on private anticompetitive conduct. As the U.S. Supreme Court has repeatedly observed, the U.S. Constitution's federalism, and indeed the Constitution itself, were designed largely as a response to the destructive interstate competition for economic activity, most notably in the form of "customs barriers and other economic retaliation,"[11] that characterized the pre-Constitutional period: "If 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."[12]

THE U.S. LEGAL SYSTEM'S LIMITATIONS ON STATE INTERFERENCE WITH AN OPEN NATIONAL COMMON MARKET ARE CONCEPTUALIZED AS ASPECTS OF THE CONSTITUTIONAL FRAMEWORK OF FEDERALISM.

At the heart of the Constitution's response to state interference with an open economy is the Commerce Clause, which delegates to the federal government the power to "regulate Commerce . . . among the several states."[13] Although the words of the clause speak only of an affirmative grant of authority to the U.S. Congress, the framers understood,[14] and the Supreme Court has consistently recognized,[15] that it served an equally important negative or dormant function, as a prohibition against state measures that interfere with or seek to constrain interstate economic activity for local advantage. Indeed, while the Commerce Clause has proven a fertile source of a very wide range of federal legislative activity (including, among a great many others, the federal antitrust laws), only rarely has

10 *See, e.g.,* City of Columbia v. Omni Outdoor Advertising, Inc., 499 U.S. 365 (1991).

11 Baldwin v. G.A.F. Seelig, Inc., 294 U.S. 511, 522 (1935) (quoting 2 THE RECORDS OF THE FEDERAL CONVENTION OF 1787, at 308 (Max Farrand ed., revised ed. 1937)).

12 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)).

13 U.S. CONST., art. I, § 8, cl. 3.

14 *See* 3 THE RECORDS OF THE FEDERAL CONVENTION OF 1787, at 478 (James Madison explaining that the Commerce Clause "was intended as a negative and preventive provision against injustice among the States themselves").

15 *See, e.g., Baldwin*, 294 U.S. at 522.

Congress exercised its Commerce Clause authority specifically to rein in state interference with interstate commerce. By contrast, the courts have applied the dormant Commerce Clause with great frequency to invalidate state measures that impermissibly infringed the free flow of interstate commerce, whether through regulation or through taxation.

Among the primary subjects of the courts' attention, dating back into the nineteenth century, have been the recurrent efforts of the states to use their tax systems to provide preferential treatment for in-state economic activity. Tariffs are, of course, the paradigm for such measures, although, as the Supreme Court has observed, "tariffs . . . are so patently unconstitutional that our cases reveal not a single attempt by any State to enact one."[16] Instead, the Court has reviewed a vast array of other types of state tax measures that touched on interstate commerce to determine whether they impermissibly interfered with the Commerce Clause's common-market goals.

In this long history, the Court's efforts to set appropriate limits on state taxation have deployed a wide range of different, and at times inconsistent, approaches.[17] 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."[18]

For the past thirty years, the Court has adopted a relatively stable analysis for Commerce Clause challenges to state tax measures, which assesses a challenged measure's practical effects against a four-prong test. The Court's long-standing,

16 West Lynn Creamery v. Healy, 512 U.S. 186, 193 (1994).

17 For a helpful overview of this tortuous history, *see* Walter Hellerstein, *State Taxation of Interstate Business: Perspectives on Two Centuries of Constitutional Adjudication*, 41 TAX LAW 37, 38-50 (1987).

18 Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 329 (1977) (internal quotations and citations omitted).

anti-discrimination principle is one of the four prongs, and remains the one of primary relevance for measures that favor or reward in-state economic activity.[19] Indeed, over the past three decades, the Court has deployed the anti-discrimination principle to invalidate more than a dozen different state tax strategies that provided preferential treatment for in-state activity or in-state actors.

The types of measures that the Court has struck down as discriminatory are diverse. *Bacchus Imports, Ltd. v. Dias* invalidated a Hawaii provision that exempted certain locally produced alcoholic beverages from an otherwise generally applicable liquor excise tax.[20] *Boston Stock Exchange v. State Tax Commission* found unconstitutional a New York stock transfer tax that provided preferential rates for transfers that were executed on New York stock exchanges, rather than on out-of-state markets.[21] *Westinghouse Electric Corp. v. Tully*, struck down a measure, again from New York, that granted a credit against the state's corporate income tax measured by the share of the company's export business that was conducted in New York.[22] *Fulton Corp. v. Faulkner* overturned a North Carolina property tax which reduced the tax on ownership of corporate shares as the percentage of the corporation's business that was located in North Carolina increased.[23]

The Court's concept of what constitutes discrimination is straightforward: "'discrimination' simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter."[24] A primary focus in determining whether a particular tax provision runs afoul of the anti-discrimination principle is a practically oriented analysis of the provision's purposes and effects. If an underlying purpose of a provision is to advantage local commerce or local activities, or if a natural consequence of the measure is to distort tax-neutral decisions about where to do business or to "exert [ ] an inexorable hydraulic pressure" favoring in-state activity, these are each strong indicia of discrimination.[25] In this analysis, the Court directs a particularly critical eye towards

19 *See* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977). The *Complete Auto* test requires that a tax "is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State."

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

21 Boston Stock Exchange v. State Tax Commission, 429 U.S. 318 (1977).

22 Westinghouse Electric Corp. v. Tully, 466 U.S. 388 (1984).

23 Fulton Corp. v. Faulkner, 516 U.S. 325 (1996).

24 Oregon Waste Sys., Inc. v. Dep't of Envtl. Quality, 511 U.S. 93, 99 (1994).

25 *See, e.g., Bacchus Imports*, *supra* n. 20, at 263, 270-73; *Boston Stock Exch.*, *supra* n. 21, at 331; American Trucking Ass'ns v. Scheiner, 483 U.S. 266, 286 (1987).

provisions that discriminate "on their face," which the Court deems "virtually per se invalid."[26] While the Court has never offered a precise definition of facial discrimination, the measures to which it has assigned this label are those where the differential treatment of in-state and out-of-state activity is evident in the language of the operative tax statute.

It is important to observe that the Court's anti-discrimination principle requires two distinct elements: both differential treatment and a resultant benefit for in-state activity. If a measure does not provide for distinctive treatment of in-state and out-of-state activity, then the mere fact that the measure may have the effect or purpose of encouraging in-state activity does not render it discriminatory. For instance, a generally applicable reduction of business tax rates or an exemption of business personal property from property taxation surely has the effect, and likely the purpose, of encouraging local investment, but such measures do not treat out-of-state activity in less favorable ways, and nothing in the Court's Commerce Clause jurisprudence suggests that such measures raise any hint of forbidden discrimination. Indeed, the Court has repeatedly observed that "it is a laudatory goal in the design of a tax system to promote investment that will provide jobs and prosperity to the citizens of the taxing State."[27] The Commerce Clause only forbids those efforts that seek to achieve these legitimate ends by improper means, means which discriminate in their treatment of in-state and out-of-state activity. As the Court explained in *Boston Stock Exchange*, "in the process of competition no State may discriminatorily tax the products manufactured or the business operations conducted in any other State."[28]

III. The Commerce Clause Applied to State Location Incentives

To what extent does the Supreme Court's anti-discrimination jurisprudence set limits to the proliferating efforts of the states to use their tax systems to provide incentives for in-state investment? At the least, many of the tax incentive measures which have become commonplace in recent years invite serious questions of their validity under the Commerce Clause. So, it is perhaps surprising that the Supreme Court has not had the occasion to address the constitutionality of any of the characteristic tax incentives that have been broadly adopted by the states.

The likely explanation lies in the fact that the Court can only address cases that parties bring to it. And the typical parties who litigate Commerce Clause challenges to state tax measures are out-of-state or interstate businesses who are

26 *See, e.g., Fulton Corp., supra* n. 23, at 325, 331.

27 Trinova Corp. v. Michigan Dep't of Treasury, 498 U.S. 358, 385-86 (1991).

28 *Boston Stock Exch.*, 429 U.S. at 337.

disfavored by the benefits that a challenged measure provides to their in-state competitors. But such businesses are typically receiving the benefit of similar incentives in the states where their plants or other activities are located; so, they would be ill-advised to bring a challenge which, if successful, might well kill the goose that is laying their golden eggs.

In its recently concluded 2005 term, the Supreme Court finally did take a case, *DaimlerChrysler Corp. v. Cuno*, in which the U.S. Court of Appeals for the Sixth Circuit had found that Ohio's investment tax credit violated the Commerce Clause.[29] But this case was brought, not by a business competitor, but by a group of local taxpayers, both individuals and small businesses, who challenged the tax credit because of its negative impact on the state's tax revenues and the resultant impact on them in the form of higher taxes and reduced state services. The Supreme Court concluded that such plaintiffs did not have the requisite personal stake in the litigation to satisfy the requirements for standing to sue in the federal courts, and therefore the Court did not reach the merits of the Commerce Clause claim. Although the plaintiffs remain free to—and intend to—pursue their claim in the state courts, which apply their own, more permissive, rules concerning standing to sue,[30] the outcome in the Supreme Court indicates some of the hurdles (to which we return below) that stand in the way of a definitive ruling on the constitutionality of the more widespread state incentives.

Nonetheless, a number of state tax measures whose purpose or effect is to encourage or reward in-state business location decisions have been reviewed by the courts, and they have repeatedly been found to violate the anti-discrimination principle. The Supreme Court has struck down New York's incentives for locating export activity in the state,[31] North Carolina's property tax breaks for shareholders of companies that expand their in-state presence,[32] and a Louisiana severance tax credit that favored in-state mineral extraction,[33] in each case focusing on the fact that the preference for in-state activity would impermissibly encourage businesses to locate new investment in the state. In addition to the

29 126 S. Ct. 1854 (2006) (vacating 386 F.3d 738 (6th Cir. 2004)). In the interests of full disclosure, I note that I represented the citizen plaintiffs in this case before both the U.S. Court of Appeals for the Sixth Circuit and the U.S. Supreme Court, and continue to represent them in their forthcoming state court suit.

30 In fact, the plaintiffs had initiated the original suit in the Ohio state courts, partly because of concerns about federal rules concerning standing. The case was removed to federal court by the defendants, over plaintiffs' objections. Defendants only attacked plaintiffs' standing after the plaintiffs' victory on the merits before the Court of Appeals.

31 *Westinghouse Electric, supra* n. 22.

32 *Fulton Corp., supra* n. 23.

33 Maryland v. Louisiana, 451 U.S. 725, 756-57 (1981).

Sixth Circuit's decision invalidating Ohio's investment tax credit,[34] other appellate courts have struck down a New York City provision providing accelerated depreciation limited to assets placed in service in the city,[35] an exemption from Pennsylvania's capital stock tax that was designed to encourage in-state location of manufacturing facilities,[36] and a Nevada sales tax exemption limited to air carriers that located their central offices in the state.[37]

As these cases suggest, many of the characteristic state tax incentives used to reward in-state investment are vulnerable to a straightforward and compelling application of the Supreme Court's anti-discrimination reasoning. Consider, for example, an investment tax credit (ITC), like the one challenged in the *Cuno* case, one of the most ubiquitous forms of location incentive. An ITC allows a business to reduce its state income tax by a specified percentage of the cost of new facilities, machinery, or equipment acquired or placed in service in the taxing state. States impose a variety of restrictions on the classes of property or types of businesses eligible for the credit, but they all restrict the credit to investments in property located and used within the state.

Because of this locational restriction, an ITC discriminates in precisely the way that the anti-discrimination principle forbids. Its differential treatment of in-state and out-of-state economic activity is evident. Compare two otherwise identically situated businesses, each of which is subject to the state's income tax on an identical portion of its income. If one now builds a new facility in the state and the other builds an identical facility elsewhere, the first will be entitled to a credit against its state income tax, while the other will not.[38]

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34 Cuno v. DaimlerChrysler Corp., 386 F.3d 738 (6th Cir. 2004), *vacated on other grounds*, 126 S. Ct. 1854 (2006).

35 R.J. Reynolds Tobacco Co. v. Dep't of Fin., 667 N.Y.S.2d 4 (N.Y. App. Div. 1997).

36 PPG Indus. v. Commonwealth, 790 A.2d 252 (Pa. 1999).

37 Worldcorp. v. Dep't of Taxation, 944 P.2d 824 (Nev. 1997). One arguable exception to this pattern is Caterpillar, Inc. v. Dep't of Treasury, 488 N.W.2d 182 (Mich. 1992), which upheld a Michigan tax preference for in-state capital investment, but the ruling in that case depended heavily on the unique features of Michigan's single business tax.

38 Of course, because of the new investments, the two companies are no longer identically situated. Defenders of state ITCs have suggested that, since the in-state location of a new plant will increase the proportions of the company's property and payroll located in the state and will thereby increase the proportion of the company's income taxable in the state under many states' apportionment rules, the ITC might be justified as merely compensating for the tax increase attendant on the plant location. In fact, however, in almost any realistic scenario, the tax savings from an ITC will vastly exceed any added tax burden from the new plant's in-state location. And, in any case, the ITC's differential effect will remain evident in the different effective tax rates that the two hypothetical companies will pay on the share of their incomes apportioned to the state under the state's (presumably legitimate) apportionment methods, with the in-state company paying a lower effective rate than its out-of-state competitor.

Nor is there any question that the effect of the ITC is to give an advantage to in-state investment, thereby encouraging businesses to locate their new facilities in the state. As the Sixth Circuit explained in *Cuno*, concerning Ohio's ITC:

> "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."[39]

Thus, the practical effect of the ITC is to "encourage [ ] the development of local industry by . . . impos[ing] greater burdens on economic activities taking place outside the State than were place[d] on similar activities within the State."[40] In short, the ITC precisely fits the Supreme Court's definition of forbidden discrimination: it constitutes "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter."[41] And, since the discrimination is expressly set forth in the language of the ITC statutes, when they restrict the credit to investments located in the taxing state, state ITCs are apt to be found "virtually per se unconstitutional."

This outcome should come as no surprise, because, in fact, an ITC serves as the functional equivalent of a tariff on out-of-state manufacturers. Were a state to tax two different businesses, each of which sold its products in the state, at different rates based on where the goods were manufactured, with the in-state manufacturer paying a lower rate than its out-of-state competitor, we would have a classic instance of a forbidden tariff.[42] But this is precisely the effect that an ITC accomplishes, albeit by somewhat different means. After all, a credit that is available only on the basis of in-state investment reduces the effective tax rate of those businesses with in-state facilities, just as an explicitly lower tax rate would.

39 *Cuno*, *supra* n. 34, at 743.

40 *Westinghouse Electric*, *supra* n. 22, at 404.

41 *Oregon Waste*, *supra* n. 24, at 99.

42 Perhaps it might be argued that a classic tariff would operate as a tax on the sales (i.e., on the gross revenue from the transactions) rather than on the apportioned net income of the competing companies. But, as the Supreme Court has emphasized in applying the anti-discrimination principle to a corporate income tax, "It cannot be that a State can circumvent the prohibition of the Commerce Clause against placing burdensome taxes on out-of-state transactions by burdening those transactions with a tax that is levied in the aggregate . . . rather than on individual transactions." *Westinghouse Electric*, *supra* n. 22, at 404.

Indeed, since ITCs are often large enough to offset a business's entire state income tax liability for a period of years after they locate a substantial manufacturing facility in the state, an ITC can convert an otherwise neutral income tax on manufacturers into a tariff that applies only to those competitors who manufacture outside the state. Thus, it should come as no surprise that a number of commentators describe ITCs as paradigmatic examples of tax breaks that violate the Commerce Clause.[43]

The same anti-discrimination argument will also reach a wide range of the other tax incentives currently in use by the states. Other locationally based credits against corporate income taxes, such as targeted jobs credits which are measured by a company's new employment in the taxing jurisdiction, are susceptible to precisely the same analysis as ITCs. Or, to take a somewhat different example, consider the increasingly common use of property tax exemptions that are conditioned on a specified level of new employment at the exempted facility or on other forms of in-state activity. As noted earlier, no one would suggest that a simple exemption of a certain class of assets from property taxation would offend the Commerce Clause. Since the state does not—indeed, cannot—tax comparable out-of-state properties, its decision not to tax the in-state properties does not discriminate in favor of the in-state investments.

But, if the property tax exemption is conditioned on some additional form of in-state activity, such as a specified level of in-state employment, the provision becomes discriminatory. Here, the discrimination is not between a business with in-state property and a competitor with out-of-state property, but rather between two businesses with in-state property, one of whom commits to the requisite level of in-state employment (or other in-state activity on which the property exemption is conditioned) and the other of whom concentrates its new employment out-of-state (or is unable or unwilling to commit to the required level of in-state activity). Here, as with the ITC, the tax provision expressly favors the business engaging in in-state activity over a comparably situated competitor who does not, by exempting the property of the one from taxation, while taxing the property of the other.

Several judicial decisions have found such location-based conditions on otherwise non-discriminatory tax exemptions to violate the Commerce Clause. For example, the Supreme Court struck down a Maine property tax exemption for charitable organizations, because the exemption was available only to those organizations which primarily served in-state residents.[44] Similarly, the U.S.

43 *See, e.g.,* Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 817-18 (1996); Peter D. Enrich, *Saving the States from Themselves: Commerce Clause Constraints on State Tax Incentives for* Business, 110 HARV. L. REV. 377, 434-37 (1996); Robert D. Plattner, *State Business Tax Incentives: Are They Vulnerable to Constitutional Attack*, ST. TAX TODAY 128-19 (Jul. 3, 2000).

44 Camps Newfound/Owatonna v. Town of Harrison, 520 U.S. 564 (1997).

Court of Appeals for the Fifth Circuit invalidated a Louisiana provision which conditioned property tax exemptions for new industrial facilities on the taxpayer's agreement to give preference to in-state suppliers, contractors, and labor in the construction and operation of the exempted facility.[45] And the Sixth Circuit, in *Cuno*, despite finding that the particular property tax exemption challenged in that case was not unconstitutional, emphasized that "an exemption may be discriminatory if it requires the beneficiary to engage in another form of business in order to receive the benefit or is limited to businesses with a specified economic presence," although it found that the particular conditions imposed on the challenged exemption did not cross those thresholds.[46]

Thus, a wide range of location-based tax incentives appear vulnerable to Commerce Clause invalidation. The primary stratagem of defenders of such incentives in responding to such arguments has been to suggest that the Supreme Court's anti-discrimination case law can, and should, be read more narrowly, in a manner that would not reach typical investment incentives of the sort discussed above. In particular, they argue that the Supreme Court has only invalidated state tax provisions as discriminatory when they either function as tariffs levied directly on interstate transactions or impose tax penalties on businesses for their out-of-state activities.[47] The suggestion, then, is that measures like ITCs or conditional property tax exemptions are unproblematic, since they do not apply against transactional taxes and since they provide tax reductions (i.e., benefits) for in-state activity, rather than tax increases (i.e., penalties) for out-of-state activity.

As I and other commentators have explained at greater length elsewhere,[48] however, this argument's critical distinction between tax benefits and penalties cannot withstand scrutiny. Not only are its proponents unable to cite a single case in which the Court has deployed such a distinction, but in fact the Court has expressly, and quite sensibly, disavowed any meaningful distinction between tax benefits and burdens:

45 Pelican Chapter, Associated Builders & Contractors, Inc. v. Edwards, 128 F.3d 910 (5th Cir. 1997). *See also* Worldcorp v. Dep't of Taxation, 944 P.2d 824 (Nev. 1997) (invalidating a Nevada sales tax exemption because it was restricted to purchasers who located their central office in the state).

46 *Cuno*, *supra* n. 34, at 746.

47 This attempted categorization had its origins in Philip Tatarowicz & Rebecca Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 Vand. L. Rev. 879 (1986), and has been adopted by a number of more recent commentators and litigants.

48 *See* Enrich, *supra* n. 43, at 444-446; Hellerstein & Coenen, *supra* n. 43, at 813-15; Respondents' Brief at 39-43, DaimlerChrysler, Inc. v. Cuno, 126 S. Ct. 1854 (2006) (No. 04-1704).

> "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."[49]

Indeed, several of the Court's anti-discrimination decisions fail to fit within the argument's narrow categories, because they invalidate measures which operate as benefits for in-state activity rather than as burdens on out-of-state activity.[50] And, were the courts to adopt the purported benefits/penalties distinction, they would reintroduce precisely the type of formalistic distinction that the Supreme Court's practically oriented Commerce Clause jurisprudence has sought to eschew, and would invite states to revive a wide range of forbidden measures by simply recasting them in technically different form. In short, the benefits/penalties distinction is not supported by "either the decisions themselves, or the underlying purposes of the Commerce Clause."[51]

IV. Shortcomings of the Commerce Clause as a Constraint

At present, judicial enforcement of the Commerce Clause's anti-discrimination principle appears to be the only viable legal restraint on the states' proliferating competition to offer ever-more generous tax incentives to reward businesses for locating their facilities in the state.[52] Nonetheless, neither the doctrinal parameters of Commerce Clause law nor reliance on the courts to enforce these constitutional limits on the states are without their difficulties. In this closing section, I briefly canvass several shortcomings of this approach, relating both to the content of the applicable doctrine and to the institutional roles implicated in reliance on judicial enforcement.

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49 *Bacchus Imports*, *supra* n. 20, at 273.

50 *See Westinghouse Electric*, *supra* n. 22, 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."); Maryland v. Louisiana, *supra* n. 33, at 757; *American Trucking*, *supra* n. 25; *Camps Newfound, supra* n. 12.

51 Hellerstein & Coenen, *supra* n. 43, at 815.

52 One other possible source of legal restraint, which is beyond the scope of this article, lies in U.S. trade treaty commitments, to the extent that they constrain subsidization of domestic industry. For one introduction to the possible arguments, *see* WILLIAM SCHWEKE & ROBERT K. STUMBERG, COULD ECONOMIC DEVELOPMENT BECOME ILLEGAL IN THE NEW GLOBAL POLICY ENVIRONMENT? (Corporation for Enterprise Development, 1999).

A. THE MARKET-PARTICIPANT EXCEPTION

While the courts have enforced the dormant Commerce Clause broadly as a limit on state and local tax and regulatory measures that discriminate against interstate business activity, the Supreme Court has sharply circumscribed the range of state and local actions that are subjected to Commerce Clause scrutiny. In particular, the Court has drawn a bright line between measures it characterizes as market regulation and those it views as market participation. The former category, which encompasses taxation and enactment of governmental rules and standards that apply to private businesses, warrants rigorous judicial review for potential conflicts with the federal power to "regulate Commerce . . . among the several states." But the latter category, which encompasses governmental execution of its own operations and programs, is completely immunized from Commerce Clause analysis, on the theory that governments, just like private market actors, should be free to choose with whom they do business and on what terms. Thus, the Court has found that the Commerce Clause does not apply to a city's decision to require its contractors to employ local residents[53] or to a state's choice to sell cement produced by a state-owned plant at discriminatory rates favoring in-state purchasers.[54]

JUDICIAL ENFORCEMENT OF THE COMMERCE CLAUSE'S ANTI-DISCRIMINATION PRINCIPLE APPEARS TO BE THE ONLY VIABLE LEGAL RESTRAINT ON THE STATES' PROLIFERATING COMPETITION TO OFFER EVER-MORE GENEROUS TAX INCENTIVES TO REWARD BUSINESSES FOR LOCATING THEIR FACILITIES IN THE STATE.

In consequence of this "market-participant exception," a wide range of the non-tax measures that states commonly use to reward business location decisions, such as providing worker training or infrastructure improvements, assembling sites, or offering low-cost loans, are likely not to be susceptible to judicial scrutiny, regardless of the degree to which they may tilt the playing field in favor of in-state investment. Indeed, it can be argued that even a direct cash subsidy paid to a business would fall within the protected sphere of market participation, although the Court has been careful to note that it has never addressed or decided the constitutionality of direct subsidies.[55] Thus, while some types of state location incentives are subject to close Commerce Clause scrutiny, others, indistinguishable in their financial value to the recipient businesses, are not scrutinized at all.

53 White v. Massachusetts Council of Constr. Employers, 460 U.S. 204 (1983).

54 Reeves, Inc. v. Stake, 447 U.S. 429 (1980).

55 *See* West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 199 n.15 (1994). Despite the Court's disclaimer in *West Lynn*, one of the leading market-participant cases, *Hughes v. Alexandria Scrap Corp*., 426 U.S. 794 (1976), involved state payments of incentive "bounties" to in-state scrap dealers, payments which look quite similar to simple subsidies, although the Supreme Court characterized them as state participation in the market for the processing of abandoned vehicle hulks. *See also* New Energy Co. v. Limbach, 486 U.S. 269, 277 (1988) (noting that *Alexandria Scrap*'s reasoning may not apply to typical subsidy programs).

This differential treatment of financially equivalent incentives constitutes a troubling anomaly, particularly in light of the Court's asserted focus on the "practical effects" of state measures that favor in-state economic activity. Of course, beyond their simple financial valuation, there are a number of significant differences between tax breaks and cash incentives, which make the use of tax breaks more attractive both to governments and to businesses, and which may justify closer scrutiny of the former than the latter. From the governmental perspective, tax breaks are typically far more readily enacted, without the need to compete in the annual appropriations process and with far less transparency; from the business perspective, they smack far less of governmental hand-outs.

Still, defenders of state tax incentives against Commerce Clause invalidation often underscore the foolishness of interpreting the Constitution to ban one kind of measure when states can, and do, deliver precisely the same financial rewards by other means, free of any constitutional constraint. And at least one commentator has suggested that the arbitrariness of the distinction between cash incentives and tax breaks reveals the bankruptcy of the Court's entire anti-discrimination jurisprudence and argues for judicial withdrawal from the field.[56]

Of course, nothing in the Commerce Clause or in the Court's anti-discrimination framework dictates the blanket insulation of all forms of preferential governmental spending from Commerce Clause scrutiny that the market-participant case law suggests. The European Court of Justice, in addressing a comparable issue in defining impermissible "state aid," has deployed a far narrower and more nuanced "market investor" test, which insulates state measures from treatment as state aid only if the resultant advantage for the local business is one which might similarly have been obtained from a private business behaving "under normal market conditions."[57]

Perhaps it is the relative infrequency with which American governments—as contrasted with their European counterparts—have historically participated directly in commercial markets that has invited and rendered viable a broad-brush immunity from Commerce Clause scrutiny for all forms of market participation. And perhaps, with the growing scale of state interventions in the market in favor of local economic activity, the U.S. Supreme Court will move toward an approach to market participation more like the EC Court's. Indeed, the Court's caution not to pre-judge the question of whether direct subsidies constitute market participation, and its recent references to the "narrow exception" for market

56 *See* Edward A. Zelinsky, *Restoring Politics to the Commerce Clause: The Case for Abandoning the Dormant Commerce Clause Prohibition on Discriminatory Taxation*, 29 OHIO N.U. L. REV. 29 (2002).

57 *See* Kelyn Bacon, *The Concept of State Aid: The Developing Jurisprudence in the European and UK Courts*, 2003 EUR. COMPETITION L. REV. 54, 55 (quoting Case C-256/97 Demenagements-Manutention Transport, 1999 E.C.R. I-3913, 1999 C.M.L.R. 1, 22).

participants,[58] may presage such a development. But, in the meanwhile, the Court's bright-line market-participant exception limits the efficacy and cogency of its anti-discrimination jurisprudence.

B. ANTI-DISCRIMINATION'S UNDER- AND OVER-BREADTH

Even within the more limited confines of tax incentives, the Court's focus on whether a measure discriminates in its treatment of in-state and out-of-state activity is an imperfect tool for singling out those tax measures used by the states to lure businesses in violation of common-market norms. In fact, as discussed above, a number of commonly used incentive measures, such as abatements of property taxes for new plants or remission of sales taxes on new machinery and equipment, are generally non-discriminatory (absent any location-based strings attached to the tax benefits) because they involve taxes that simply are not applicable to out-of-state activity. But such provisions are largely indistinguishable, in their economic effects on both businesses and states, from their discriminatory counterparts. Similarly, the Court has concluded that a state's use of a so-called "single sales factor" income apportionment formula, which looks exclusively to the location of the taxpayer's sales in determining what share of the taxpayer's income the state can tax (contrary to what the Court has recognized as the benchmark approach which averages the proportions of a taxpayer's property, payroll, and sales in the state), does not discriminate in favor of in-state production,[59] notwithstanding the rapid proliferation of the single sales factor methodology as a leading location incentive and protectionist device.

Conversely, the anti-discrimination principle threatens to invalidate a range of tax breaks that are intended to serve purposes quite distant from competing for interstate business, but which are nonetheless conditioned on some type of in-state activity. For example, at the oral argument in *Cuno*, Chief Justice Roberts asked whether the Commerce Clause would forbid homestead exemptions from local property taxes, since such exemptions—because they are typically restricted to a taxpayer's primary residence—are limited to homeowners who are in-state residents. Similar concerns might be raised, for example, about state tax credits for the installation of pollution abatement equipment, which are unsurprisingly restricted to equipment installed at facilities in the taxing state. Perhaps it can be argued that such measures, in practical fact, have neither the intent nor the effect of providing an economic advantage to in-state economic activity, or perhaps they can be defended on the basis of their obvious and substantial non-discriminatory purposes. Still, the suggestion that such provisions facially discriminate between in-state and out-of-state economic activity, and thus should be found "virtually per se unconstitutional," is plausible enough to raise serious concerns about whether the anti-discrimination principle is too broad.

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58 *See, e.g.*, *Camps Newfound*, *supra* n. 12, at 589.

59 *See* Moorman Mfg. Co. v. Bair, 437 U.S. 267, 277-79 (1978).

These failings of the anti-discrimination principle reflect the difficult challenge that the courts face in attempting to articulate a workable test for impermissible state interference with interstate economic activity. Such a test must draw a reasonably definite line along a murky continuum. On one end of the continuum are tariffs, which directly and exclusively tax out-of-state production and which the Constitution surely sought to forbid; at the other end are state choices about what sorts of taxes to impose and at what rates, decisions which surely fall within the legitimate sphere of state autonomy in a federalist system. In between them lies a virtually infinite array of possible ways that a state can modify elements of its tax system to create a more favorable economic climate or to reduce the burdens of taxation on local businesses.

All of the measures along the continuum can potentially be seen as interfering with the free flow of economic activity in the national common market, since all of them can affect (and are commonly designed to affect) business choices about where to locate. To enable the Commerce Clause to serve as a workable judicial constraint on measures at one end of the continuum, while not intruding on those at the other end, the Supreme Court has settled on the anti-discrimination principle as a way of drawing an intelligible line between the presumptively permissible and the presumptively unconstitutional measures, a line that identifies differential treatment of in-state and out-of-state activity as the critical threshold that states cannot cross. And, while other elements of the Court's Commerce Clause jurisprudence have been repeatedly revised and reversed, this element has remained a steady and generally effective standard for more than a century. While far from perfect, it may be as good a simple standard as courts can devise.

C. LIMITATIONS ON THE JUDICIAL ROLE

Aside from these difficulties with the doctrinal framework that the courts have developed to assess challenged state tax incentives, reliance on the courts as the enforcers of constitutional limits on state efforts to favor in-state activity is itself problematic in a number of respects. Courts can only intervene in particular cases, challenging specific state actions or measures, and can only do so at the instigation of parties who are willing and able to invoke the courts' jurisdiction. The result is, at best, a rather episodic and haphazard oversight of state efforts to further their parochial interests.

One particularly significant difficulty, already alluded to above, arises from restrictions on judicial standing, that is, on who has the right to bring a case in the courts. While many state courts take more liberal approaches to standing, the federal courts require plaintiffs to have a direct and personal relationship to the challenged action, in the form of a direct injury, which is distinct from injuries suffered by the general public, and which will be alleviated by the requested judicial intervention. Thus, the federal courts are generally unreceptive to challenges to state taxing and spending policies that are brought by citizens or taxpayers whose interest is simply to protect the state fisc from unconstitutional

expenditures or losses of revenue. As was noted earlier, in *Cuno*, for example, the reason that the Supreme Court declined to reach the question of the constitutionality of Ohio's investment tax credit and vacated the Sixth Circuit's finding of unconstitutionality was that the citizens and small businesses who brought the challenge did not allege an injury that was "concrete and particularized," but instead asserted a grievance that they suffered "in some indefinite way in common with people generally."[60]

Limitations on standing do not bar all potential challengers of state tax incentives from access to the courts. Most of the past Commerce Clause anti-discrimination cases in the federal courts were brought by businesses who were not receiving the benefits of favorable tax treatment available to their competitors, and such competitors certainly would have standing to challenge location incentives that favored their in-state competition.[61] In addition, a state would most likely have standing to challenge an incentive measure offered by another state, which threatened to encourage businesses to shift their activity away from the state bringing the suit.[62] But, at present, neither competing businesses nor states seem promising potential plaintiffs. The businesses are typically receiving comparable tax benefits from the states where they have located their activity, and will be cautious about endangering those benefits as well as their continuing ability to obtain new tax breaks in connection with future decisions, while states are hesitant to bring a challenge which would likely invalidate some of their own incentives, along with those of other states. And, while citizen plaintiffs may often have access to state courts, with their typically more permissive standing rules, the restrictive federal standing doctrine will preclude them from appealing an unfavorable state court ruling to the Supreme Court.[63]

These standing barriers—and the disinclination, on the part of those who do have standing, to challenge a status quo from which they benefit—probably explain the paucity of case law applying the well-established, anti-discrimination

60 DaimlerChrysler Corp. v. Cuno, *supra* n. 48, at 1854, 1862. In fact, many of the plaintiffs in *Cuno* had indeed suffered a direct and personal injury, since they had lost their homes and businesses to make way for the new plant, but, because these injuries would not have been redressed by a judicial ruling invalidating the tax incentives, those injuries were irrelevant to their standing.

61 For one recent example of such a case, see *Northwest Airlines, Inc. v. Wisconsin Dept. of Revenue*, 717 N.W.2d 280 (Wis. 2006), where Northwest challenged a property tax incentive limited to airlines with a hub in Wisconsin. If Northwest seeks Supreme Court review of the state supreme court's decision, standing will be no obstacle.

62 *See, e.g.* Wyoming v. Oklahoma, 502 U.S. 437 (1992).

63 If citizen plaintiffs should win a Commerce Clause challenge in the state courts, the Supreme Court would not be barred from reviewing that decision, on the request of the state or an affected business taxpayer. *See* ASARCO Inc. v. Kadish, 490 U.S. 605 (1989). This is one plausible route by which this issue may ultimately find its way to the Supreme Court, although state courts are likely to be less sympathetic than federal courts to challenges to their own states' tax provisions and hence less likely to reach decisions that would open the door to Supreme Court review.

principle to the wide range of state business tax incentives that have become so common in recent decades. And they raise serious doubts about the efficacy of judicial intervention as a way to set meaningful limits to the continued proliferation of state incentives.

Moreover, even when a successful case is pursued through the courts, the result is limited to the invalidation of the particular incentive challenged in that case. A judicial decision does not, by its own force, affect even quite similar measures in place in other jurisdictions, and states will be quick to argue, as they did in the wake of the Sixth Circuit decision in *Cuno* invalidating Ohio's ITC, that their comparable provisions are significantly distinguishable from the invalidated measure. If the judicial decision comes from a court of limited geographic jurisdiction (that is to say, from any court other than the Supreme Court), the arguments for the decision's inapplicability to other states' measures will only be reinforced. Thus, at least the short-term effect of judicial invalidation of a state tax incentive will likely be to take a tool out of the hands of one state while leaving comparable tools in the hands of many others, a result that hardly furthers the Commerce Clause goal of placing the states on a level playing field. In addition, long experience with judicial enforcement of Commerce Clause limits on state tax measures suggests that invalidation of one type of measure only spurs the states to devise new and different techniques to achieve comparable effects, techniques whose unconstitutionality can only be tested when proper parties step forward to bring yet another lawsuit. Case-by-case adjudication is a clumsy tool for enforcing a national free trade tax policy.

D. RESIDUAL CONGRESSIONAL AUTHORITY

The courts' role as enforcers of Commerce Clause limits on state actions is, of course, a derivative one. The Commerce Clause is primarily a grant of regulatory authority over interstate commerce to Congress, and the courts only deploy the dormant Commerce Clause in the absence of congressional action. It is well-established that, whatever the courts may do in the face of legislative silence, Congress retains the power not only to regulate interstate commerce by affirmative measures, and not only to forbid particular forms of state discrimination against interstate commerce, but also to delegate particular aspects of its authority over interstate commerce to the states, and thereby to authorize them to engage in conduct, even discriminatory conduct, which would, absent congressional authorization, be found unconstitutional.[64]

64 *See, e.g.,* Western & Southern Life Ins. Co. v. State Bd. of Equalization, 451 U.S. 648 (1981) (construing McCarran-Ferguson Act as granting states plenary power to regulate insurance industry and thereby as authorizing discriminatory state taxation of insurance companies).

Exercising its Commerce Clause authority, Congress has occasionally enacted specific prohibitions on discriminatory state taxation.[65] And it has included a number of restrictions on state measures designed to influence business location decisions as conditions on participation in federally funded economic development programs.[66] Some critics of the proliferation of state location incentives have called for federal legislation as the preferred way to halt or limit the interstate competition, and bills have occasionally been filed in Congress to forbid certain kinds of location incentives, or to impose federal taxes that would negate their benefits.[67]

In the present political climate, however, congressional intervention is far more likely on the opposite side—to protect the ability of states to offer tax incentives to reward in-state economic activity. In fact, in the immediate wake of the Sixth Circuit's decision invalidating Ohio's investment tax credit, the senators from the states in the Sixth Circuit (Ohio, Michigan, Tennessee, and Kentucky) filed legislation to override the court's ruling, reflecting their concern that the ruling, unless and until reviewed by the Supreme Court, would place their states at a competitive disadvantage by taking out of their hands, but not competing states' hands, some of the key tools for influencing business location decisions. In the subsequent congressional session, a broader coalition of senators and congressmen filed a far more comprehensive bill (S. 1066) that would broadly authorize the states, with limited exceptions, "to provide . . . for economic development purposes tax incentives that otherwise would be the cause or source of discrimination against interstate commerce under the Commerce Clause."[68]

The effect of this legislation would be to turn the present federal approach to discriminatory state tax measures on its head. Now, discriminatory provisions are presumed to be unconstitutional, unless they can be shown necessary to serve an important non-discriminatory state purpose. But under the provisions of S. 1066, the so-called "Economic Development Act," discriminatory measures would be presumed to be permissible, so long as they were intended for economic development purposes, unless they fell within one of the Act's specific exceptions, which were crafted to avoid overruling a number of the Supreme Court's prior cases.

65 *See, e.g.,* 42 U.S.C. § 11503 (barring discriminatory state taxation of railroad property).

66 *See, e.g.,* 26 U.S.C. § 1391(d)(1)(F) (imposing "anti-piracy" conditions on federal designation of empowerment or enterprise zones, eligible for favorable federal tax treatment).

67 *See, e.g.,* Melvin L. Burstein & Arthur J. Rolnick, *Congress Should End the Economic War Among the States*, 9 REGION 3 (1995) (Federal Reserve Bank of Minneapolis Annual Report); Daniel Shaviro, *An Economic and Political Look at Federalism in Taxation*, 90 MICH. L. REV. 895, 975-88 (1992).

68 S. 1066, 109th Cong. § 2 (2005). Identical legislation, H.R. 2471, 109th Cong. (2005), was filed in the House of Representatives. For further discussion of this proposed legislation, *see Cuno and Competitiveness: Where to Draw the Line: Hearing Before the Subcomm. on International Trade of the S. Comm. on Finance*, 109th Cong., 2nd Sess. (Mar. 16, 2006), *available at* http://finance.senate.gov/sitepages/hearing031606.htm.

Before the Supreme Court's decision vacating the Sixth Circuit's decision in the *Cuno* case, S. 1066 had attracted wide and vocal support, both from powerful segments of the business community and from major groups representing state policymakers, such as the National Governors Association. It was widely anticipated that, had the Court affirmed the lower court's invalidation of Ohio's investment tax credit, the pressure for speedy congressional enactment would have been intense. Instead, the effect of the Court's decision in *Cuno* was to slow the momentum behind the bill substantially. But its sponsors and supporters remain committed to its eventual enactment, and their political clout remains an important reminder of the severe institutional limits on the use of the courts to constrain the economic competition among the states.

V. Conclusion

Thus, reliance on judicial enforcement of the Commerce Clause's anti-discrimination principle to rein in the states' inevitable tendencies to favor their parochial economic interests suffers from a number of serious shortcomings, both doctrinal and institutional. Nonetheless, over much of the nation's history, the courts and the dormant Commerce Clause have played a central role in combating pressures toward economic balkanization and in reinforcing the growth of an open national common market. In fact, the intensification of interstate competition for economic activity over the past few decades, and the potent political forces favoring the continuation of that competition, serve as reminders of the importance of judicially enforced constitutional constraints on these tendencies. While far from perfect, this tool has proven more effective and more dependable than the available alternatives. But, in light of its limitations, one of the key questions for those who seek to protect both the states themselves and the national economy from the harms of interstate competition over tax incentives is whether use of the courts can serve to widen public understanding of those harms and to build political support for limits on the competition.