



# Chapman Law Review

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Volume 22

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# Chapman Law Review

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## Editor's Note

It is my honor to introduce *Chapman Law Review's* first issue of volume twenty-two. We open with a response to an article published in the first issue of volume twenty-one. This current issue also consists of our "paper-only symposium," a collection of scholarly works discussing "The Commerce Clause and the Global Economy."

This issue begins with a thorough response from Professor Seth Barrett Tillman to Professor John Yoo's article, *Franklin Roosevelt and Presidential Power*. Professor Tillman discusses the often misunderstood and mischaracterized actions of President Lincoln concerning *Ex parte Merryman*. His article encourages readers to re-evaluate the oft-repeated narrative of President Lincoln's executive actions.

The symposium then opens with an introduction by Professor Frank J. Doti that provides insight into the inspiration behind the creation of this written symposium and the articles in the collection, while providing Professor Doti's own scholarly thoughts on the recent *South Dakota v. Wayfair, Inc.* decision. Following Professor Doti's introduction, are seven thought-provoking articles discussing various aspects of the Commerce Clause—or dormant Commerce Clause—and its effect on the economy within and outside of the United States.

Mr. Michael T. Fatale begins the discussion with an article focused on the Supreme Court's recent decision in *Wayfair*, and the implications of overruling the physical presence rule. Next, Professor Edward A. Zelinsky provides a comparative analysis of *Wayfair* and *Comptroller of the Treasury of Maryland v. Wynne* and discusses the future of the dormant Commerce Clause. Professor Darien Shanske examines *Wayfair* in the broader context of the Supreme Court's federalism jurisprudence and the proportionality principle. Professor Keigo Fuchi argues for the adoption of a dormant Commerce Clause counterpart in Japan and discusses the benefits from a comparative perspective. Next, Professor Tania Sebastian compares the hiring practices of India and the United States in light of the Commerce Clause within the United States and contrasts that with the lack of an equivalent clause in India. Professor F. E. Guerra-Pujol takes a unique perspective and focuses on the future impact the Supreme Court's Commerce Clause jurisprudence will have on rapidly growing

fields of technology and proposes a new approach to the Court's stare decisis principle in these areas. Mr. Louis Cholden-Brown closes out our symposium with an article examining the impact of the dormant Commerce Clause on food law and proposes that the Court refrain from balancing interests and uphold local ordinances in certain circumstances.

*Chapman Law Review* is grateful for the continued support of the members of the administration and faculty that made this written symposium and the publication of this issue possible, including: Dean of Chapman University Dale E. Fowler School of Law, Matthew Parlow; our faculty advisor, Professor Celestine Richards McConville; and our faculty advisory committee, Professors Deepa Badrinarayana, Scott Howe, Janine Kim, Ron Steiner, and Associate Dean of Research and Faculty Development, Donald Kochan. A special thank you goes to Professors Frank J. Doti and Kenneth Stahl for their assistance in formulating the concept behind this symposium and soliciting scholars. Last but not least, I would like to express my sincerest gratitude to the staff of the 2018–2019 *Chapman Law Review*—without your tireless work, this issue would not have been possible.

Amy N. Hudack  
*Editor-in-Chief*

# Merryman Redux: A Response to Professor John Yoo

Seth Barrett Tillman\*

In a recent issue of *Chapman Law Review*, Professor John Yoo wrote, “While FDR did not join *Lincoln’s blatant defiance in declining to obey a judicial order*, [Roosevelt’s] administration regularly proposed laws that ran counter to Supreme Court precedent . . . .”<sup>1</sup> My focus in this short, responsive Article is on Professor Yoo’s specific claim regarding Lincoln.

Professor Yoo’s claim is odd—isn’t it? He tells us that Lincoln passively “declin[ed] to obey a judicial order,” but also characterizes Lincoln’s passivity as “blatant defiance.”<sup>2</sup> Odd. He cites to no particular case, and he cites to no specific judicial order in any case. Very odd. We are all just supposed to know that the case was *Ex parte Merryman*,<sup>3</sup> a Civil War case, and the purported judicial order was issued by that old curmudgeon: Chief Justice Roger Brooke Taney.<sup>4</sup> In a prior publication, in 2015, Professor Yoo wrote that Lincoln had “ignored Taney’s order releasing

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\* Lecturer, Maynooth University Department of Law, Ireland. Roinn Dlí Ollscoil Mhá Nuad. University of Chicago. BA (honors); Harvard Law School, JD (*cum laude*); clerked for the United States Court of Appeals for the Third Circuit, United States District Court for the Middle District of Alabama, United States District Court for the Middle District of Pennsylvania, and the United States District Court for the District of New Jersey. I thank Professor Josh Blackman for his comments.

<sup>1</sup> John Yoo, *Franklin Roosevelt and Presidential Power*, 21 CHAP. L. REV. 215, 222 (2018) (emphasis added) (footnote omitted). Professor Yoo has a long line of scholarship making this or similar claims. See John Yoo, *Judicial Supremacy Has Its Limits*, 20 TEX. REV. L. & POL. 1, 24 (2015); John Yoo, *Lincoln and Habeas: of Merryman and Milligan and McCordle*, 12 CHAP. L. REV. 505, 513 (2009); John Yoo, *Lincoln at War*, 38 VT. L. REV. 3, 17–20 (2013); John Yoo, *Merryman and Milligan (and McCordle)*, 34 J. SUP. CT. HIST. 243, 244 (2009); see also Robert J. Delahunty & John C. Yoo, *Dream On: The Obama Administration’s Nonenforcement of Immigration Laws, the DREAM Act, and the Take Care Clause*, 91 TEX. L. REV. 781, 820 (2013).

<sup>2</sup> What would constitute “blatant defiance”? If Lincoln had ordered the Army to arrest the Chief Justice due to the latter’s having issued the *Merryman* opinion that could be fairly characterized as defiance. For a fuller discussion of what constitutes “defiance,” see Seth Barrett Tillman, *Ex parte Merryman: Myth, History, and Scholarship*, 224 MIL. L. REV. 481, 511–13 (2016). Note, several paragraphs or substantial parts of paragraphs of this Article were first published in my 2016 *Military Law Review* publication.

<sup>3</sup> See *Ex Parte Merryman*, 17 F. Cas. 144 (C.C.D. Md. 1861) (No. 9487) (Taney, C.J.); 4 A COLLECTION OF IN CHAMBERS OPINIONS BY THE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES 1400–12 (Cynthia Rapp & Ross E. Davies comps., 2004), <http://tinyurl.com/judtw8q> [<http://perma.cc/BM52-FKXU>].

<sup>4</sup> 4 A COLLECTION OF IN CHAMBERS OPINIONS, *supra* note 3, at 1400.

Merryman.”<sup>5</sup> “Ignored”—no mention of defiance here. On another occasion, in 2009, Professor Yoo characterized Lincoln’s response to *Merryman* as “outright presidential defiance.”<sup>6</sup> But here the passive language of “*ignoring*” and “*declining to obey*” was absent. Now, in 2018, Professor Yoo says it is both.<sup>7</sup> We are down the rabbit hole.

So, which is it?

[A] *Lincoln passively declined to obey a judicial order;*

[B] *Lincoln actively defied the Chief Justice; or*

[C] *Both.*

The correct answer is [D] *None of the Above.*

\*\*\*

In 2016, I made an effort to explain why the standard narrative (i.e., the narrative put forth by Professor Yoo and many others) surrounding *Merryman* is wrong. In other words, the standard restatement of the facts, reasoning, and disposition of *Merryman* appearing in many (if not most) law review articles is wrong.<sup>8</sup> Some people have noticed,<sup>9</sup> and some people (apparently)

<sup>5</sup> Yoo, *Judicial Supremacy Has Its Limits*, *supra* note 1, at 24 (emphasis added) (internal citation omitted).

<sup>6</sup> Yoo, *Lincoln and Habeas: Of Merryman and Milligan and McCardle*, *supra* note 1, at 507.

<sup>7</sup> See Yoo, *Franklin Roosevelt and Presidential Power*, *supra* note 1, at 222.

<sup>8</sup> See Tillman, *supra* note 2, at 483. I do not claim to be the first to have noticed the many significant problems with the standard legal narrative. See, e.g., *id.* at 497 n.45 (citing BRIAN MCGINTY, *THE BODY OF JOHN MERRYMAN: ABRAHAM LINCOLN AND THE SUSPENSION OF HABEAS CORPUS* 91–92 (2011); BRUCE A. RAGSDALE, *EX PARTE MERRYMAN AND DEBATES ON CIVIL LIBERTIES DURING THE CIVIL WAR* 4 (2007); JACK STARK, *PROHIBITED GOVERNMENT ACTS: A REFERENCE GUIDE TO THE UNITED STATES CONSTITUTION* 48 (2002); Frank I. Michelman, *Living with Judicial Supremacy*, 38 *WAKE FOREST L. REV.* 579, 595 n.69 (2003). See generally JONATHAN W. WHITE, *ABRAHAM LINCOLN AND TREASON IN THE CIVIL WAR: THE TRIALS OF JOHN MERRYMAN* (2011). For an entirely different approach to *Merryman*, see generally David Farnham, “*A High and Delicate Trust*”: *How Ignorance and Indignation Combined to Expand President Lincoln’s Claimed Power to Suspend Habeas Corpus in the Case of John Merryman*, 24 *J. S. LEGAL HIST.* 109 (2016).

<sup>9</sup> Prominent commentators, in law and other fields, discussing, quoting, or citing my 2016 *Military Law Review* article include: RANDY E. BARNETT & JOSH BLACKMAN, *CONSTITUTIONAL STRUCTURE: CASES IN CONTEXT* 532 & n.4 (3d ed. 2018); PAUL BREST ET AL., *PROCESSES OF CONSTITUTIONAL DECISIONMAKING: CASES AND MATERIALS* 314 n.89, 317 & n.90 (7th ed. 2018); LOUIS FISHER, *SUPREME COURT EXPANSION OF PRESIDENTIAL POWER: UNCONSTITUTIONAL LEANINGS* 41 n.124 (2017); ERIC M. FREEDMAN, *MAKING HABEAS WORK: A LEGAL HISTORY* 145 n.19 (2018); PETER CHARLES HOFFER, *UNCIVIL WARRIORS: THE LAWYERS’ CIVIL WAR* 199 n.1 (2018); MICHAEL STOKES PAULSEN ET AL., *THE CONSTITUTION OF THE UNITED STATES* 403 (3d ed. 2017); 3 WILLIAM J. RICH, *MODERN CONSTITUTIONAL LAW Conduct of the War* § 38.34 n.12 (3d ed. 2017); 1 RONALD D. ROTUNDA & JOHN E. NOWAK, *TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE AND PROCEDURE* § 6.13(b)(i) n.12 (5th ed. 2017); PETER M. SHANE ET AL., *SEPARATION OF*

have not.<sup>10</sup> The issue here is more than historical curiosity, as interesting and important as that may be. Rather, the issue here relates to the intellectual claim (made by some) that past presidents—including icons such as President Lincoln—knowingly defied or ignored (that is, “declin[ed] to obey”) federal judicial orders, and whether Lincoln’s conduct provides a model or precedent, albeit if only during war-time or other emergency. My view is that Lincoln’s *Merryman*-related conduct furnishes no such model. Here is why.

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<sup>10</sup> See, e.g., Yoo, *Franklin Roosevelt and Presidential Power*, *supra* note 1, at 222. Even post-2016, Professor John Yoo is not alone. See, e.g., RICHARD H. FALLON, JR., *LAW AND LEGITIMACY IN THE SUPREME COURT* 113 (2018) (“Lincoln oversaw and defended the defiance by Union military officers of a ruling by Chief Justice Roger B. Taney in *Ex parte Merryman*. Taney claimed the power to free an alleged Confederate collaborator in the state of Maryland, where the Union army had effectively imposed martial law and detained him without trial.” (footnote omitted)); Richard H. Fallon, Jr., *Judicial Supremacy, Departmentalism, and the Rule of Law in a Populist Age*, 96 TEX. L. REV. 487, 504 (2018) (“In *Ex parte Merryman*, Lincoln supported Union military officers in defying a writ of habeas corpus, issued by Chief Justice Roger Taney, in the early days of the Civil War.” (footnote omitted)); cf., e.g., Michael Stokes Paulsen, *The Propriety of Presidential Impeachments, Past and Present*, LAW & LIBERTY (July 19, 2018), <http://www.libertylawsite.org/2018/07/19/the-proprity-of-presidential-impeachments-past-and-present/> [<http://perma.cc/Z8QQ-TLN8>].

SHORT OVERVIEW OF *EX PARTE MERRYMAN*

The court<sup>11</sup> issued three orders in *Merryman*. But to understand what gave rise to those three judicial orders, one has to know the facts that initially brought about the litigation.

A. *Merryman*: The Facts

Following the 1860 election of Abraham Lincoln, the parade of state secession would begin. During April 1861, Fort Sumter had fallen.<sup>12</sup> Even Washington, the nation's capital, was threatened by Confederate armies, disloyal state militias, and irregular combatants, not to mention disloyal civilians, assassins, and spies. To secure the capital, President Lincoln directed Union troops to proceed to Washington through Maryland, a border state.<sup>13</sup> Mobs in Maryland had attacked Union troops; bridges and railway lines had been destroyed; telegraph wires to the capital had been cut.<sup>14</sup> Why these attacks? Why all this destruction of infrastructure? No doubt different actors had different motives. Chance and disorder—the children of mob rule—certainly played some role. But it seems likely that some (perhaps many) sought to slow down or prevent the arrival of loyal troops to secure Washington and, perhaps, to secure federal military installations in Maryland, such as Fort McHenry in Baltimore. (Certainly these were the natural, expected, and probable consequences of the attacks, even if these results were not specifically intended by the actors involved.) Lincoln responded. On April 27, 1861, in order to secure the movement of Union troops through Maryland, President Lincoln issued an order delegating authority to General Winfield Scott to suspend the writ of habeas corpus.<sup>15</sup> Lincoln's order cited no statutory basis for his decision.<sup>16</sup>

11 What court issued the decision in *Ex parte Merryman*? Some commentators say Taney was acting for the federal Circuit Court for the District of Maryland; other commentators say *Merryman* was issued as an in-chambers opinion under a special grant of authority under the Judiciary Act of 1789. I take the latter view. See A COLLECTION OF IN CHAMBERS OPINIONS, *supra* note 3, at 1400; Tillman, *supra* note 2, at 504 nn.55–56. Whatever else *Merryman* was, it was not a Supreme Court case—for that reason, I use “court,” rather than “Court” in the main text of this Article.

12 See Tillman, *supra* note 2, at 483 n.4.

13 See *id.* at 483 n.6.

14 See *id.*

15 The Constitution states: “The *Privilege* of the Writ of Habeas Corpus shall not be suspended, unless when in Cases of Rebellion or Invasion the public Safety may require it.” U.S. CONST. art. I, § 9, cl. 2 (emphasis added). President Lincoln's order, issued on April 27, 1861, only purported to give General Scott authority “to suspend the writ of habeas corpus.” See Abraham Lincoln, Order to General Scott (Apr. 27, 1861), in 6 COMPLETE WORKS OF ABRAHAM LINCOLN, 1860–1861, at 258, 258 (John G. Nicolay & John Hay eds., N.Y., The Lamb Publishing Co. new ed. 1894) (reproducing Lincoln's order); Tillman, *supra* note 2, at 527 & n.116 (same). *But see* AMANDA L. TYLER, HABEAS CORPUS



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IN WARTIME: FROM THE TOWER OF LONDON TO GUANTANAMO BAY 358 n.3 (2017) (characterizing Lincoln's April 27, 1861 order as a suspension of the "privilege"). But in his July 4, 1861 message to Congress, Lincoln recharacterized his prior order as permitting suspension of the "*privilege* of the writ of habeas corpus." Abraham Lincoln, Message to Congress in Special Session (July 4, 1861), in 6 COMPLETE WORKS, *supra*, at 297, 308 (emphasis omitted) (emphasis added). The difference between suspending the writ and suspending the privilege of the writ is night-and-day. See, e.g., *Ex parte Milligan*, 71 U.S. (4 Wall.) 2, 130–31 (1866) (Davis, J.) ("The suspension of the privilege of the writ of habeas corpus does *not* suspend the writ itself." (emphasis omitted) (emphasis added)); see also, e.g., *Ex parte Benedict*, 3 F. Cas. 159, 174 (N.D.N.Y. 1862) (No. 1292) (Hall, J.) ("Such a suspension may prevent the prisoner's discharge; but it leaves untouched the question of the illegality of his arrest, imprisonment, and deportation. If these are unlawful, the marshal and others engaged in these arrests are liable in damages in a civil prosecution; such damages to be assessed by a jury of the country."). *But cf.*, e.g., *Ex parte Zimmerman*, 132 F.2d 442, 445 (9th Cir. 1942) (Healy, J.) ("It is little to the purpose to attempt here an analysis of distinctions between suspension of the privilege and suspension of the writ."). It is not particularly surprising that these distinctions are no longer understood, as this and much else relating to the Constitution's original public meaning was forgotten even as early as Lincoln's day, and, in regard to a few constitutional provisions and language, sometimes far earlier. But it is curious how few even notice there is a puzzle to be solved or a past to be explained. See, e.g., 1 BERNARD SCHWARTZ, A COMMENTARY ON THE CONSTITUTION OF THE UNITED STATES 25 (1968) ("This *Milligan* language has been repeated in more recent cases. One may wonder, nevertheless, whether there is [a] basis for the claimed distinction between suspension of the privilege and suspension of the writ." (footnote omitted) (citing *Zimmerman*, 132 F.2d at 445)); Trevor W. Morrison, Hamdi's *Habeas Puzzle: Suspension as Authorization*, 91 CORNELL L. REV. 411, 423 n.73 (2006) ("The text of the Suspension Clause makes clear that it is the 'Privilege of the Writ,' not the writ itself, that may be suspended. . . . Nevertheless, courts and commentators tend to refer colloquially to 'suspending the writ' or 'suspending habeas,' . . ." (citing *Milligan*, 71 U.S. at 130–31)); Trevor W. Morrison, *Suspension and the Extrajudicial Constitution*, 107 COLUM. L. REV. 1533, 1535 n.3 (2007) ("[S]uspending the writ' and 'suspending habeas' are common shorthands for suspending the privilege of the writ, and I will use them here." (citing *Milligan*, 71 U.S. at 130–31)); Gerald L. Neuman, *Habeas Corpus, Executive Detention, and the Removal of Aliens*, 98 COLUM. L. REV. 961, 979 (1998) (asserting that the *Milligan* Court's "distinction [between the privilege and the writ] cuts against the conventional phrase, 'suspension of the writ,' which nonetheless has brevity in its favor"). *But see*, e.g., William Baude, *The Judgment Power*, 96 GEO. L.J. 1807, 1853 n.255 (2008) (pointing out the same textual distinction regarding the "privilege" of the writ and the writ itself, but not resolving the distinction); Jeffrey D. Jackson, *The Power to Suspend Habeas Corpus: An Answer from the Arguments Surrounding Ex parte Merryman*, 34 U. BALT. L. REV. 11, 24 (2004) ("The general consensus, even prior to the Civil War, was that suspension did not mean that habeas corpus itself was suspended, but rather that the privilege guarded by the writ was suspended." (citing WILLIAM S. CHURCH, A TREATISE ON THE WRIT OF HABEAS CORPUS 42 (photo. reprt. 1997) (1893))); Tor Ekeland, Note, *Suspending Habeas Corpus: Article I, Section 9, Clause 2, of the United States Constitution and the War on Terror*, 74 FORDHAM L. REV. 1475, 1496 (2005) ("The privilege of the writ can be construed as separate from the writ itself; the privilege may be viewed as the ends ('discharge, bail, or a speedy trial') and the writ itself as merely the means towards this end." (quoting WILLIAM F. DUKER, A CONSTITUTIONAL HISTORY OF HABEAS CORPUS 141–42, 171 n.121 (1980))); Note, *Developments in the Law: Federal Habeas Corpus*, 83 HARV. L. REV. 1038, 1265–66 (1970) (denominating the *Milligan* Court's discussion of the Suspension Clause's "privilege of the writ" language as "cryptic," and suggesting that "the [*Milligan*] Court saw the 'privilege' as the further proceedings and the eventual discharge. By the 'writ' the Court meant what is referred to today as a show cause order, *i.e.*, not an order to produce the body but a preliminary request for a 'return,' or written justification of the detention." (footnote omitted)); Bautz, *supra* note 9 *passim* (collecting some early authorities addressing the distinction). Compare, e.g., Emily Calhoun, *The Accounting: Habeas Corpus and Enemy Combatants*, 79 U. COLO. L. REV. 77, 121–22 n.216 (2008) (citing *Milligan* for the proposition

that habeas jurisprudence distinguishes executive accountability goals from remedial goals and phases of habeas litigation), *with* John Harrison, *The Original Meaning of the Habeas Corpus Suspension Clause 3* (University of Virginia School of Law Public Law & Legal Theory Paper Series 2018-47, Aug. 23, 2018), <https://www.ssrn.com/abstract=3227985> (“A suspension of the privilege of the writ of habeas corpus is legislation granting the executive extremely broad discretion to detain.”), *with id.* at 40 (“[T]he privilege of the writ of habeas corpus is the legal interest that the writ characteristically protects. To suspend that privilege is to contract that legal interest temporarily.”), *with* Lee Kovarsky, *Prisoners and Habeas Privileges under the Fourteenth Amendment*, 67 VAND. L. REV. 609, 614–15 (2014) (“The privilege is a prisoner’s entitlement to ask that the habeas power be exercised.”), and Amanda L. Tyler, *Is Suspension A Political Question*, 59 STAN. L. REV. 333, 396–97 (2006) (conflating the initial and subsequent phases of habeas litigation, but still citing *Milligan* without explanation).

My view is that suspension of the *evidentiary* privilege of the writ of habeas corpus precludes a court (or even an Executive Branch officer) from taking cognizance of a party’s *pleading* (or invoking) the writ (once granted to that party by that court or any other court of record) in subsequent contempt and enforcement proceedings (and, perhaps, in other collateral and ancillary proceedings). For example, *Merryman II* (i.e., granting an order to serve an attachment for contempt where the defendant failed to produce the prisoner-plaintiff). Suspending the writ (as opposed to suspending the privilege of the writ) precludes a court from granting the writ, on the merits, in the first instance. For example, *Merryman I* (i.e., an *ex parte* habeas order to produce a prisoner), or a *Merryman III*-like order (i.e., a habeas order to release a prisoner—albeit, of course, this did not actually happen in *Merryman*). When both the writ and/or the privilege of the writ are suspended, federal courts (having general federal question jurisdiction) will still have jurisdiction to determine if the suspension or suspensions themselves are constitutional—unless Congress has validly stripped the federal courts of jurisdiction to do so. The scope of Congress’s power to engage in such jurisdiction stripping is a complex subject, and one well beyond the scope of this Article. *See, e.g.*, Henry M. Hart, Jr., *The Power of Congress to Limit the Jurisdiction of Federal Courts: An Exercise in Dialectic*, 66 HARV. L. REV. 1362, 1398 (1953) (“[W]here statutory jurisdiction to issue the writ obtains, but the privilege of it has been suspended in particular circumstances, the Court has declared itself ready to consider the validity of the suspension and, if it is found invalid, of the detention.”); Edward A. Hartnett, *The Constitutional Puzzle of Habeas Corpus*, 46 B.C. L. REV. 251, 289 (2005). *See generally* Battaglia v. Gen. Motors Corp., 169 F.2d 254 (2d Cir. 1948) (Chase, J.). Recently, the Suspension Clause has received renewed interest and full-length treatment in books, but the meaning of the clause’s text, its actual words—they remain largely an undiscovered country. *See generally, e.g.*, TYLER, *supra*, at 3–4, 15, 99, 123, 133, 359 (taking a historical approach absent textual analysis); Amanda L. Tyler, *Suspension as an Emergency Power*, 118 YALE L.J. 600, 678 n.372 (2009) (citing Neuman, *supra*, at 979 favorably). *But see, e.g.*, Baude, *supra*, at 1853 n.255; *but cf., e.g.*, Bautz, *supra* note 9 *passim*.

I have put down some truly remarkable support for my position here in another paper which this Article is too small to contain. *Cf.* Seth Barrett Tillman, *A Play on the Suspension Clause*, NEW REFORM CLUB (Aug. 11, 2016, 4:04 PM), <https://reformclub.blogspot.com/2016/08/a-play-on-suspension-clause.html> [<http://perma.cc/HP6M-YTBJ>]. Indeed, I submitted a prior draft of this lengthy footnote as my abstract to the Tenth Annual Originalism Works-in-Progress Conference. *See Tenth Annual Hugh & Hazel Darling Foundation Originalism Works-in-Progress Conference*, UNIVERSITY OF SAN DIEGO SCHOOL OF LAW (last visited July 27, 2018), [http://www.sandiego.edu/events/law/detail.php?\\_focus=66934](http://www.sandiego.edu/events/law/detail.php?_focus=66934) [<http://perma.cc/RXD9-FA8C>]; *see also* Seth Barrett Tillman, *What is the “Privilege” of the Writ of Habeas Corpus?*, NEW REFORM CLUB (July 27, 2018, 2:41 AM), <https://tinyurl.com/ycupmlu7> [<http://perma.cc/Y695-PLGV>].

<sup>16</sup> *See* Tillman, *supra* note 2, at 485. Here and throughout this Article, I quote freely from my 2016 *Military Law Review* publication. *See id.* at 483–85.



## B. *Merryman I*: The Ex Parte Order to Produce the Prisoner

John Merryman was from a long-established land-owning and politically connected Maryland family, as was his wife. At the outbreak of the Civil War, he had already been elected to public office as a member and president of the Baltimore County Commission.<sup>17</sup> Rightly or not, federal military authorities suspected John Merryman of being an officer of a pro-secession militia group which allegedly had conspired to destroy (and did destroy) bridges and railway lines. As a result, at around 2:00 AM, on Saturday, May 25, 1861, United States Army personnel seized Merryman, and they subsequently transferred him to and detained him at Fort McHenry in Maryland.<sup>18</sup> The next day—Sunday, May 26, 1861—Merryman’s Maryland counsel, George M. Gill and George H. Williams, presented Merryman’s habeas corpus petition to Chief Justice Roger Brooke Taney at the Chief Justice’s Washington home.<sup>19</sup> Later that day, Sunday, May 26, 1861, the Chief Justice issued an ex parte order, *Merryman I*, directing General George Cadwalader, the only named defendant and the Army officer having overall command of the military district including Fort McHenry: (i) to appear before Chief Justice Taney the next day—on Monday, May 27, 1861 at 11:00 AM—in a court room in Baltimore; (ii) to explain the legal basis for Merryman’s detention by military authorities; and (iii) to “produce”<sup>20</sup> (as opposed to “release”) the body of John Merryman at that hearing.<sup>21</sup>

The writ, i.e., *Merryman I*, was issued by Chief Justice Taney and served by the United States Marshal on General Cadwalader the same day: Sunday, May 26, 1861, at around 5:30 PM.<sup>22</sup> The hearing was scheduled for Monday, May 27, 1861, at 11:00 AM. As a result, Cadwalader, a Pennsylvania native, had less than one full business day: (i) to consult (much less coordinate) with the United States Attorney for Maryland, with the Attorney General in Washington, and with the Army’s law officers; and (ii) to find a private attorney in the Maryland bar to represent his personal interests in high-stakes litigation.<sup>23</sup> As a result, it is not entirely surprising that Cadwalader chose not to attend the May 27, 1861 hearing. Instead, he sent Colonel R. M. Lee.<sup>24</sup> At the hearing, Colonel Lee presented the court with a

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<sup>17</sup> *See id.* at 485 & n.11.

<sup>18</sup> *See id.* at 487 & n.13.

<sup>19</sup> *See id.* at 488 & n.14.

<sup>20</sup> *Ex parte Merryman*, 17 F. Cas. 144, 145 (C.C.D. Md. 1861) (No. 9487) (Taney, C.J.).

<sup>21</sup> *See* Tillman, *supra* note 2, at 488.

<sup>22</sup> *See id.* at 499 n.47.

<sup>23</sup> *See id.*

<sup>24</sup> *See id.* at 512 n.73.

signed response from Cadwalader laying out the General's defense. For example, Cadwalader argued that habeas corpus had been lawfully suspended under presidential authority. Cadwalader's response also sought a postponement to seek additional direction from the President if the court should determine that Cadwalader's defense was insufficient. Furthermore, Cadwalader did not produce Merryman at the hearing as he was instructed to do by Chief Justice Taney's *ex parte* order.<sup>25</sup>

### C. *Merryman II*: The Attachment

Because General Cadwalader, the named defendant, failed to produce Merryman, Chief Justice Taney, on May 27, 1861, directed the United States Marshal to serve an attachment for contempt on Cadwalader.<sup>26</sup> The Marshal sought to serve the attachment on the morning of Tuesday, May 28, 1861 at Fort McHenry, but the Marshal was not admitted. *Many at the time, including perhaps Chief Justice Taney and others since, believed, and continue to believe, that this was a Cromwellian civilian-military confrontation.*<sup>27</sup> In other words, the military authorities prevailed not as a matter of established legal right as determined by the courts, but because the Army (which was acting under the direction of the President) had greater firepower than the United States Marshal (who was serving the attachment order under instructions from the Chief Justice). As a result, the Marshal left the Fort.<sup>28</sup> He reached the courthouse prior to noon on May 28, 1861, and he came without Cadwalader and Merryman.<sup>29</sup>

### D. *Merryman III*: The Final Order

In his opinion, Chief Justice Taney expressed the view that the President had no unilateral power to suspend habeas corpus. In other words, under the Constitution, only Congress can suspend habeas corpus. He also took the position that “[a] military officer has no right to arrest and detain a person not subject to the rules and articles of war, for an offence against the laws of the United States, except in aid of the judicial authority, and subject to its control.”<sup>30</sup> For those reasons, he concluded: “It is, therefore, very

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<sup>25</sup> *See id.* at 489–90.

<sup>26</sup> *See id.* at 490.

<sup>27</sup> *See id.*

<sup>28</sup> *See id.* at 491 n.25.

<sup>29</sup> *See id.* at 490–91.

<sup>30</sup> *Merryman*, 17 F. Cas. 144, 145 & 147 (C.C.D. Md. 1861) (No. 9487) (Taney, C.J.).

clear that John Merryman, the petitioner, is entitled to be set at liberty and discharged immediately from imprisonment.”<sup>31</sup>

Noting that his attachment order, *Merryman II*, “ha[d] been resisted by a force too strong for me [Taney] to overcome,”<sup>32</sup> Chief Justice Taney’s final judicial order did not command Cadwalader, Lincoln, the Army, or anyone else to release Merryman. Instead, Chief Justice Taney’s final order directed the clerk of the Circuit Court for the District of Maryland to transmit a copy of the proceedings and his opinion to President Lincoln, where it would “remain for that high officer, in fulfilment of his constitutional obligation to ‘take care that the laws be faithfully executed,’ to determine what measures he will take to cause the civil process of the United States to be respected and enforced.”<sup>33</sup> Merryman was not released as a consequence of Chief Justice Taney’s decision, nor was he brought before a military tribunal. Instead, Merryman remained detained at Fort McHenry until he was transferred to the federal civilian authorities, and then he was indicted for treason in the District Court for Maryland on July 10, 1861. He was released on bail on or about July 13, 1861. Merryman was never brought to trial.<sup>34</sup>

Again, Chief Justice Taney delivered an oral opinion on May 28, 1861, which ended live proceedings in court. Subsequently, on Saturday, June 1, 1861, he filed an extensive written opinion. The written opinion was put on file with the United States Circuit Court for the District of Maryland.<sup>35</sup>

Chief Justice Taney’s final order (not his opinion) stated:

I shall, therefore, order all the proceedings in this case, with my opinion, to be filed and recorded in the [C]ircuit [C]ourt of the United States for the [D]istrict of Maryland, and direct the clerk to transmit a copy, under seal, to the [P]resident of the United States. It will then remain for that high officer, in fulfilment of his constitutional obligation to “take care that the laws be faithfully executed,” to determine what measures he will take to cause the civil process of the United States to be respected and enforced.<sup>36</sup>

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<sup>31</sup> *Id.* at 147; Tillman, *supra* note 2, at 492.

<sup>32</sup> *Merryman*, 17 F. Cas. at 153.

<sup>33</sup> *Id.* (quoting the Take Care Clause).

<sup>34</sup> See Tillman, *supra* note 2, at 493.

<sup>35</sup> See *id.* at 491–92.

<sup>36</sup> *Merryman*, 17 F. Cas. at 153 (quoting the Take Care Clause) (emphasis added). This is the order as reported in *Federal Cases*. The report of the order in the case’s file (storing the original documents) in the Maryland state archives is even more limited than what is reported in *Federal Cases*. See *1 June 1861, Order that opinion be filed and recorded in the Circuit Court of the United States for the District of Maryland, directing the Clerk transmit a copy under seal to the President of the United States*, ARCHIVES OF MARYLAND (BIOGRAPHICAL SERIES): JOHN MERRYMAN (1824–1881) (last visited July 13, 2018), <https://msa.maryland.gov/megafile/msa/speccol/sc3500/sc3520/001500/001543/html/casepapers.html>.

In short, Chief Justice Taney's final judicial order, *Merryman III*, did not command Cadwalader or anyone else to release Merryman. Instead, Chief Justice Taney's final order meekly directed the clerk of the Circuit Court for the District of Maryland merely to transmit a copy of the proceedings and his (i.e., the Chief Justice's) opinion to President Lincoln.<sup>37</sup> The express language of the order itself left it to the President to determine the scope of his own response.

As explained, Professor Yoo's claim is that "Lincoln's [conduct amounted to] blatant defiance in declining to obey a judicial order."<sup>38</sup> To be clear, Professor Yoo's claim is not that Cadwalader, Lincoln's military subordinate, disobeyed a court order. (Such a claim would be true: Cadwalader did disobey *Merryman I*: the ex parte order—albeit, Cadwalader's conduct can be explained as consistent with standard practices in the context of ex parte temporary restraining orders.<sup>39</sup>) Nor is Professor Yoo's claim that Lincoln authorized the suspension of the writ of habeas corpus *prior* to Merryman's seizure by the Army. (Such a claim would be true: Lincoln, in fact, did authorize such a suspension—albeit, its legal validity can be questioned.) Rather, Professor Yoo's claim is that *after* Chief Justice Taney issued an order (*Merryman I*, *Merryman II*, and/or *Merryman III*), Lincoln "declin[ed] to obey" it, and that such inactivity can be fairly characterized as "blatant defiance."

The only defendant in *Merryman* was General Cadwalader. Lincoln was not a named party in *Merryman*. Lincoln was not served with process. Lincoln had no meaningful notice and opportunity to be heard during the judicial proceedings while they were ongoing.<sup>40</sup> Indeed, there is no good evidence that Lincoln even knew of the proceedings until May 30, 1861—after live judicial proceedings had ended on May 28, 1861.<sup>41</sup> Likewise, Lincoln would not have received the final order, *Merryman III*, along with Chief Justice Taney's written opinion, from the clerk of the court, until on or after June 1, 1861, when the final order was signed and filed with the circuit court—again all after live judicial proceedings had ended on May 28, 1861.<sup>42</sup> As a general rule, a stranger to a lawsuit—a non-party—a person who had no opportunity to be

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<sup>37</sup> See Tillman, *supra* note 2, at 492.

<sup>38</sup> Yoo, *Franklin Roosevelt and Presidential Power*, *supra* note 1, at 222.

<sup>39</sup> See Tillman, *supra* note 2, at 515–18.

<sup>40</sup> See *id.* at 495 n.44.

<sup>41</sup> Albeit, it is possible that Lincoln read newspaper reports of *Merryman* on the evening of May 27, 1861 or that Lincoln received correspondence from Army law officers as early as the 27th. Neither of which amounts to *notice and the opportunity to be heard* in the sense of how that phrase is ordinarily used. See *id.* at 500 n.49.

<sup>42</sup> See *id.* at 498–500, 499 n.48, 537.

heard—is not bound to obey any judicial order issued in such a lawsuit.<sup>43</sup> As a non-party, Lincoln no more “ignored” or “declin[ed] to obey” the three judicial orders in *Merryman* than did Jefferson Davis, or you, or me.<sup>44</sup> Suggesting that Lincoln “defi[ed]” such an order is strange, and characterizing Lincoln’s conduct as “blatant defiance” is stranger still. If the thrust of Professor Yoo’s claim was that Lincoln had been in privity<sup>45</sup> with Cadwalader, and for that reason accountable for Cadwalader’s conduct or culpable for his (i.e., Lincoln’s) own failure to conform to Chief Justice Taney’s orders, such an argument has yet to be made by Professor Yoo or by anyone else.

I suspect that the real gravamen of Professor Yoo’s position is not that Lincoln was a party (or in privity with a party) and formally bound by the orders as a party (or privy) might be.<sup>46</sup> Rather, I suspect that Professor Yoo’s position is that, under the Take Care Clause, President Lincoln, as General Cadwalader’s ultimate superior at the top of the chain of command, had ongoing supervisory responsibility for Cadwalader’s conduct—before, during, and after the conclusion of *Merryman*.<sup>47</sup> Is it really so obvious that a superior’s failure to supervise a subordinate, where the subordinate acts lawlessly, should be characterized as “defiance,” much less “blatant defiance”? If this is Professor Yoo’s position, it is, at the very least, undertheorized. What the exact scope of the President’s duties (if any) under the Take Care Clause remains unsettled even today—it was certainly unsettled in 1861—and even assuming that any judicially cognizable duties (as opposed to abstract, non-justiciable, or aspirational political obligations) flow from that constitutional provision, any such duties must have been greatly attenuated under the conditions faced by Lincoln during a political crisis and a hot civil war. Characterizing Lincoln’s conduct as “blatant defiance,” and making that charge stick, requires more, much more, than Professor Yoo’s *ipse dixit*.

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<sup>43</sup> See *Martin v. Wilks*, 490 U.S. 755, 761 (1989) (Rehnquist, C.J.); see also *D’Arcy v. Ketchum*, 52 U.S. (11 How.) 165, 176 (1850) (Catron, J.).

<sup>44</sup> In 2016, after some six hours of closely proofreading the penultimate draft of my *Military Law Review* article with me, my Irish legal research assistant left my office and said: “I am going home now—where I intend to ignore the Chief Justice’s order.” See Tillman, *supra* note 2, at 481 n.\* (thanking Paul Brady LLB). He got it.

<sup>45</sup> See generally *Martin*, 490 U.S. *passim*.

<sup>46</sup> There is no occasion to address whether Lincoln violated Chief Justice Taney’s opinion. Even assuming that one can defy an opinion, whatever that might mean, Professor Yoo has made no such claim. Professor Yoo’s article spoke of declining to obey and defying a judicial order, not an opinion. See Edward A. Hartnett, *A Matter of Judgment, Not a Matter of Opinion*, 74 N.Y.U. L. REV. 123, 126 (1999) (“The operative legal act performed by a court is the entry of a judgment; an opinion is simply an explanation of reasons for that judgment.”).

<sup>47</sup> See U.S. CONST. art. II, § 3 (Take Care Clause).

Finally, which order does Professor Yoo think Lincoln “declin[ed] to obey” and “blatantly def[ied]”? As to *Merryman I* and *Merryman II*, by May 30, 1861, when Lincoln first had a report of the case,<sup>48</sup> live judicial proceedings had already ended and actual compliance with these preliminary orders (as written) was no longer feasible. It was no longer possible to “produce” John Merryman at the hearing—which is what *Merryman I* demanded—because the hearing had already ended. Likewise, once the final order had been issued, once litigation had ended, *Merryman II*—the attachment for civil contempt—was a legal nullity.<sup>49</sup> More importantly, compliance was no longer possible: the attachment order demanded that Cadwalader appear before Chief Justice Taney on May 28, 1861, at noon. After May 28, 1861, compliance with this order—as written—was no longer possible. What about *Merryman III*? Did Lincoln “decline to obey” or “blatantly defy” that order? The simple answer is “no.” Again, Lincoln was not a party—so he had no obligation to obey any order. More importantly, the order did not direct Lincoln (or anyone else) to take any specific course of conduct in regard to John Merryman (or any other habeas applicant).<sup>50</sup> So any critique of Lincoln’s conduct based on his (purported) passively failing to obey or his (purported) actively “defy[ing],” much less “blatantly defy[ing],” the *Merryman III* order, makes little sense. To be clear, this interpretation of *Merryman III*, i.e., that Lincoln could not have defied the order because no concrete relief was awarded, is not some modern invention. This view was well understood by Lincoln’s contemporaries. During the Civil War, judges, other than Chief Justice Taney, sitting on federal and state courts, self-consciously followed the *Merryman* precedent, which they understood as granting the habeas applicant no concrete relief.<sup>51</sup> Likewise, in responding to President Lincoln’s and the public’s concerns surrounding *Merryman*, Attorney General Bates’s July

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<sup>48</sup> Lincoln received a report from the United States Attorney for Maryland on May 30, 1861. See Tillman, *supra* note 2, at 499 n.48.

<sup>49</sup> See *id.* at 523 & n.103; Philip A. Hostak, Note, International Union, United Mine Workers v. Bagwell: A Paradigm Shift in the Distinction Between Civil and Criminal Contempt, 81 CORNELL L. REV. 181, 185 & n.26 (1995) (“[I]f the underlying controversy giving rise to a civil contempt action is settled or is otherwise terminated, the contempt proceeding becomes moot, and the sanctions must end.” (citing *Gompers v. Buck’s Stove & Range Co.*, 221 U.S. 418, 452 (1911) (Lamar, J.))).

<sup>50</sup> See Tillman, *supra* note 2, at 492.

<sup>51</sup> See *Ex parte McQuillon*, 16 F. Cas. 347, 348 (S.D.N.Y. 1861) (No. 8294) (Betts, J.) (“[Judge Betts] would, however, follow out that case [*Merryman*], but would express no opinion whatever, as it would be indecorous on his part to oppose the [C]hief [J]ustice. He would therefore decline taking any action on the writ at all.” (emphasis added)); *In re Kemp*, 16 Wis. 359, 371 (1863) (Dixon, C.J.) (“I deem it advisable, adhering to the precedent set by other courts and judges under like circumstances, and out of respect to the national authorities, to withhold [granting habeas relief] until they shall have had time to consider what steps they should properly take in the case.” (emphasis added)).



5, 1861 memorandum only addressed the President's obligations in situations analogous to *Merryman I*, i.e., the ex parte preliminary production order. On its face, Bates's memorandum did not address final orders like *Merryman III*.<sup>52</sup> There was simply no need to do so because Lincoln's conduct in relation to the final judicial order was legal in all respects, and obviously so.

Academics should welcome debate—even when our own views are subjected to the closest scrutiny and critique. But when our views are contradicted, with novel argument and new evidence, our response ought not be to continue as if nothing has changed. Now it may be that the new *Merryman* narrative,<sup>53</sup> and I, have failed (and will continue to fail) to convince Professor Yoo. But if that is so, I hope he will tell us (or, at least, me) why. If I have convinced him, I would urge him to tell his audience: all those who have swallowed the *Merryman*-red-pill-to-historical-&-legal-wonderland. Of course, there is a third possibility—Professor Yoo is not sure. And that would be the most interesting result of all.

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<sup>52</sup> Suspension of the Privilege of the Writ of Habeas Corpus, 10 Op. Att'y Gen. 74 (July 5, 1861) (Bates, A.G.). Bates's memorandum addressed two questions:

1. In the present time of a great and dangerous insurrection, has the President the discretionary power to cause to be arrested and held in custody, persons known to have criminal intercourse with the insurgents, or persons against whom there is probable cause for suspicion of such criminal complicity?
2. In such cases of arrest, is the President justified in refusing to obey a writ of *habeas corpus* issued by a court or a judge, requiring him or his agent to produce the body of the prisoner, and show the cause of his caption and detention, to be adjudged and disposed of by such court or judge?

*Id.* at 75 (emphasis added).

<sup>53</sup> See *supra* note 8 (collecting authorities).





# Introduction:

## Withering Stare Decisis

*Frank J. Doti\**

We had just started our second year of law school. Our challenging Constitutional Law professor, James Marshall, told us to read and brief a recent U.S. Supreme Court decision about state tax law not yet in our case book. My buddies and I were not enamored with Constitutional Law. Plus requiring us to study a constitutional law/tax case was disconcerting.

The case was *National Bellas Hess v. Department of Revenue of Illinois*<sup>1</sup>. Bellas Hess was a mail-order company based in Missouri selling goods in the Midwest, including in Illinois. The consumers in Illinois would place orders by mail to the Missouri base of operations. Illinois imposed a sales tax on Bellas Hess for all of its sales delivered to Illinois consumers. Bellas Hess refused to pay, claiming it was not doing business in Illinois.

After we discussed the case in class, Professor Marshall concluded that the Court developed a very important limitation on the power of states to tax interstate sales: The Court required that a seller have a physical presence in the taxing state.<sup>2</sup> Bellas Hess had no employees, office, warehouse, or any other physical presence in Illinois related to its business. Thus, the Court held that Illinois could not tax Bellas Hess. To do so would be an unconstitutional interference and burden on interstate commerce.<sup>3</sup> The tax also adversely affected the due process protections to Bellas Hess.<sup>4</sup>

This made sense to me and my fellow law students. In fact, it still seems like a fair and reasonable U.S. constitutional rule of law. The Framers wanted to keep commerce flowing freely among the states.<sup>5</sup> To impose a tax on an out-of-state retailer who is a

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<sup>1</sup> 386 U.S. 753 (1967). The following facts are a summary of the case. *See generally id.*

<sup>2</sup> *See id.* at 756–60.

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> *See, e.g.*, U.S. CONST. art. 1, § 8, cl. 3.

remote seller would improperly burden its ability to economically conduct business across state lines.

Now I am a Chapman University Dale E. Fowler School of Law professor teaching and researching contract and taxation laws. I heard about Justice Kennedy questioning the *Bellas Hess* and *Quill Corp. v. North Dakota*<sup>6</sup> physical presence requirement in his concurring opinion in *Direct Marketing Ass'n v. Brohl*.<sup>7</sup> I knew it would not take long for a state to be enticed to impose and enforce collecting a tax on out-of-state remote sellers without having any physical presence in the state.

Leave it to a relatively low populated state, South Dakota, to test the waters on Justice Kennedy's tease.

Captivated by all this, I recommended to our law review editors and faculty advisor to consider devoting our 2019 *Chapman Law Review* to explore the legal ramifications of a leading case up for oral arguments in spring 2018—*South Dakota v. Wayfair*.<sup>8</sup>

We are doing just that. The U.S. Supreme Court ruled in *Wayfair* that the physical presence requirement is wrong and overruled *Bellas Hess* and *Quill*.<sup>9</sup> All of the Justices believed that the technological advances brought about by the Internet caused out-of-state sellers to have too dramatic an impact on lost state tax revenue.<sup>10</sup> South Dakota limited its sales tax to out-of-state sellers with annual sales exceeding \$100,000 or 200 individual sales.<sup>11</sup> Any remote sellers exceeding the thresholds would be required to collect and pay sales taxes.<sup>12</sup>

In a dissent authored by Chief Justice Roberts, the dissenting Justices also felt the physical presence test was no longer proper.<sup>13</sup> Nevertheless, the four dissenters held that they were precluded by stare decisis to overrule *Bellas Hess* and *Quill*.<sup>14</sup> Why change a rule of law that flourished for more than 50 years? Thus, they agreed with *Wayfair, Inc.* because the South Dakota tax improperly taxes a remote seller without a physical presence in the taxing state.

I am fascinated by the impact of the close 5-4 majority decision in *Wayfair* on internet sales by large marketers such as

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<sup>6</sup> 504 U.S. 298 (1992).

<sup>7</sup> 135 S. Ct. 1124 (2015).

<sup>8</sup> 138 S. Ct. 2080 (2018).

<sup>9</sup> *Id.* at 2099.

<sup>10</sup> *See id.* at 2085.

<sup>11</sup> *Id.* at 2089.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 2101 (Roberts, C.J., dissenting).

<sup>14</sup> *Id.*

eBay. Obviously, eBay meets the more than \$100,000 per year sales threshold required by the majority, if its auction sales are counted. But eBay is a huge online auctioneer marketing goods on behalf of many occasional sellers.

Say an individual has a small collection of rare major league autographed baseballs. This seller has an eBay account and sells through eBay three baseballs in separate sales totaling \$800 during the calendar year. The seller is not above the \$100,000 or over the 200 sales requirements. Under *Wayfair* it appears that the seller should not have to charge and collect an out-of-state sales tax. But will eBay have to charge and collect the tax because eBay itself is well over the threshold? In my opinion, eBay should not collect the tax, since it is not the seller of the goods. It is really an agent for the actual occasional seller. Yet the court did not have to address this and many other issues. Litigation is expected to follow, unless Congress quickly enacts legislation detailing the power of states to tax internet sales.

My above issue and many more have brought together our guest scholars in researching and writing about a fascinating area of law. As a tax law specialist, I am pleased to have a combination U.S. constitutional and taxation related subject matter at the forefront of current legal news.

Shortly after our law school opened in 1997, I came up with the idea of devoting our annual law review issues to cutting edge topics on a distinct subject with a complementary live symposium. We were in 1998 and looked forward to entering the new millennium. Our first topic orientated law review was on federal tax policy in the new millennium. Since then we have continued the distinct topic law review approach. I was honored to author the introduction of the first such law review in 1999. I am especially honored to it do again twenty years later.

We present in this issue the Commerce Clause limitations on state interstate taxation and linked dormant Commerce Clause jurisprudence.

Mr. Louis Cholden-Brown studies the Commerce Clause from a different perspective. He explores the dormant Commerce Clause retrenchment. Mr. Cholden-Brown focuses on recent California and Massachusetts laws banning the sale of eggs, pork, and veal from animals raised in cruel conditions. He is a Senior Advisor, New York City 2019 Charter Revision Commission.

Mr. Michael T. Fatale studies the *Wayfair* decision by telling us what the U.S. Supreme Court believes is the more appropriate standard for limitations on state taxation of interstate commerce. He also explains the confusing aspects of

the opinion to states and taxpayers. Mr. Fatale is the Deputy General Counsel of the Massachusetts Department of Revenue and is an adjunct professor at Boston College of Law. He was the lead speaker at the February 14, 2019 Chapman University Dale E. Fowler School of Law live seminar exploring *Wayfair* and its impact on interstate taxation.

Professor Keigo Fuchi gives us a Japanese perspective on how *Wayfair* and our Commerce Clause limitation on state taxation is a useful doctrine. Professor Fuchi believes that Japan could use a comparable legal framework from a comparative law perspective. Professor Fuchi is a professor of law at Kobe University Graduate School of Law.

Professor F. E. Guerra-Pujol considers the impact of *Wayfair* on bitcoin transactions. He questions if technological advances justify the Court's departure from the physical presence rule. Professor Guerra-Pujol is a professor of business law at the University of Central Florida.

Professor Tania Sebastian turns to an analysis of our Commerce Clause. She studies its affect in connection with hiring practices and preferences in the Unites States compared to India. Professor Sebastian points out the basic difference between our federalism form of government compared to the combination of federal and unitary regimes in India. Professor Sebastian is an assistant professor of law at VIT Chennai Campus School of Law.

Professor Darien Shanske considers the *Wayfair* decision in the context of federalism jurisprudence. Professor Shanske argues that the Court felt compelled to restore the reality of the need for state financing through interstate taxation. Professor Shanske is a professor of law at UC Davis School of Law.

Professor Edward A. Zelinsky compares the dormant Commerce Clause law in the U.S. Supreme Court decisions in *Wayfair* and *Maryland v. Wynne*. He concludes that it is unlikely that the Court will jettison the dormant Commerce Clause. But he tells us that there are nevertheless key dormant Commerce Clause skeptics on the Court. Professor Zelinsky is the Morris and Annie Trachman Professor of Law at the Benjamin N. Cardozo School of Law of Yeshiva University.

We thank our authors, *Chapman Law Review* staff, and many others who have made this issue possible. I think we should also thank the U.S. Supreme Court for again making the study and practice of law so challenging.

# Wayfair, What’s Fair, and Undue Burden

Michael T. Fatale\*

## I. INTRODUCTION

The Supreme Court’s decision in *South Dakota v. Wayfair, Inc.*<sup>1</sup> evaluated the state tax jurisdiction or “nexus” rules that apply under the so-called “dormant” aspect of the Commerce Clause.<sup>2</sup> *Wayfair* overruled, as “unsound and incorrect,” the physical presence nexus rule of *National Bellas Hess, Inc. v. Department of Revenue of Illinois*,<sup>3</sup> and *Quill Corp. v. North Dakota*,<sup>4</sup> as applied to a state use tax collection duty.<sup>5</sup> *Wayfair* concluded that this standard was inconsistent with the Court’s longstanding construction of the dormant Commerce Clause.<sup>6</sup>

*Wayfair* was a 5-4 decision featuring two concurrences that leave somewhat uncertain what part of its analysis a majority of the Justices assented to.<sup>7</sup> All nine Justices expressed antipathy to the physical presence rule. Also, there was apparently broad consensus that in the absence of the physical presence rule, state tax nexus is to be evaluated applying due process principles.<sup>8</sup> *Wayfair*, like other recent state court cases decided by the Court, illustrates that the Court continues to be concerned with state tax discrimination and a related concept, the impermissible

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\* Deputy General Counsel at the Massachusetts Department of Revenue and adjunct professor at Boston College Law School. He thanks the following persons for helpful comments submitted in connection with this Article: Richard Cram, Dave Davenport, Joe Garrett, Brett Goldberg, Brian Hamer, Helen Hecht, Phil Horwitz, Sheldon Laskin, Greg Matson, Dan Schweitzer, Shirley Sicilian and Don Twomey. This Article expresses the author’s views and not necessarily those of the Massachusetts Department of Revenue.

<sup>1</sup> 138 S. Ct. 2080 (2018).

<sup>2</sup> See U.S. CONST. art. I, § 8, cl. 3; Dep’t of Revenue of Ky. v. Davis, 553 U.S. 328, 337–38 (2008) (“The Commerce Clause empowers Congress ‘[t]o regulate Commerce . . . among the several States,’ and although its terms do not expressly restrain ‘the several States’ in any way, we have sensed a negative implication in the provision since the early days . . . [which] has come to be called the dormant Commerce Clause . . . .” (internal citations omitted)).

<sup>3</sup> 386 U.S. 753 (1967).

<sup>4</sup> 504 U.S. 298 (1992).

<sup>5</sup> *Wayfair*, 138 S. Ct. at 2099. The rule also applied to the use tax collection requirement as imposed by localities. See *Quill*, 504 U.S. at 313 n.6. In this Article, reference to the states’ use tax collection duties is intended to also reference such duties as imposed by these localities.

<sup>6</sup> See *Wayfair*, 138 S. Ct. at 2093–94. See also *infra* notes 22–26, 87–89 and accompanying text.

<sup>7</sup> See *Wayfair*, 138 S. Ct. at 2087.

<sup>8</sup> See *id.* at 2093; U.S. CONST. amend. XIV, § 1.

imposition of a double tax.<sup>9</sup> But *Wayfair* suggests that neither discrimination nor double taxation will typically be implicated when a state asserts a use tax collection duty.<sup>10</sup>

The most confusing aspect of *Wayfair* is the majority's ambivalent, vague suggestion that state tax jurisdiction can also be evaluated utilizing the dormant Commerce Clause principle of "undue burden."<sup>11</sup> Undue burden is an inquiry that derives from the 1970 case, *Pike v. Bruce Church, Inc.*,<sup>12</sup> which pertained to a state statute that regulated commercial activity and not to the imposition of a state tax.<sup>13</sup> The *Pike* balancing test has not been applied in the state tax context and is no longer favored by the Court even in the regulatory context. *Quill* originally introduced the undue burden notion into the state tax context, but did so in a way that did not require the application of that test.<sup>14</sup> Moreover, *Wayfair* rejected the reasoning that *Quill* used to invoke *Pike*. *Wayfair* suggests that the Court itself would not actually apply the undue burden standard to the imposition of a state's use tax collection duty—and that test has no logical application with respect to other state taxes. Further, because the undue burden test has no history with respect to state taxes, it is not clear how it would be applied to such taxes.

*Wayfair's* reference to the undue burden standard seems intended to encourage states to simplify their state and local use tax collection systems as they apply to out-of-state vendors—particularly small vendors. This is certainly a laudable purpose. But the reference risks creating needless litigation and confused lower court reasoning—a consequence that would hearken back to the after-effects of *Quill*. Ironically, *Wayfair* creates this prospect even though it was critical of the litigation and confusion wrought by *Quill*.<sup>15</sup> There was no need for *Wayfair* to invoke the undue burden principle, as what the Court apparently sought to achieve could be better accomplished through a straightforward application of the Due Process Clause.

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<sup>9</sup> See, e.g., *Comptroller of Treasury of Md. v. Wynne*, 135 S. Ct. 1787 (2015). See also *Granholtz v. Heald*, 544 U.S. 460 (2005); *Am. Trucking Ass'n v. Mich. Pub. Serv. Comm'n*, 545 U.S. 429 (2005); *S. Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999); *Gen. Motors Corp. v. Tracy*, 519 U.S. 278 (1997); *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997).

<sup>10</sup> See *Wayfair*, 138 S. Ct. at 2099.

<sup>11</sup> *Id.* at 2098–99.

<sup>12</sup> 397 U.S. 137 (1970).

<sup>13</sup> See *id.* at 138; see also David S. Day, *The "Mature" Rehnquist Court and the Dormant Commerce Clause Doctrine: The Expanded Discrimination Tier*, 52 S.D. L. REV. 1, 1–2 (2007) (noting that the second aspect of the dormant Commerce Clause test applied to non-tax state regulations is "commonly referred to as the 'undue burden' standard").

<sup>14</sup> See *Quill Corp. v. North Dakota*, 504 U.S. 298, 305, 314–15 (1992).

<sup>15</sup> See *Wayfair*, 138 S. Ct. at 2092, 2097–98.



This Article proceeds in four Parts. Part One revisits the holdings and history of *Bellas Hess* and *Quill*. Part Two discusses the history and text of the South Dakota statute at issue in *Wayfair*. Part Three considers the legal theories evaluated by the Court in *Wayfair*—in particular the notions of discrimination, due process, and undue burden. Part Four offers some concluding remarks.

## II. BELLAS HESS AND QUILL

*Wayfair* overruled *Quill* and *Bellas Hess*,<sup>16</sup> both of which pertained to a state's attempt to impose a use tax collection duty on an out-of-state vendor making sales to in-state consumers.<sup>17</sup> The use tax serves as a complement to the sales tax and acts to prevent a consumer from seeking to avoid sales tax by purchasing goods outside the state.<sup>18</sup> The tax achieves this result since it applies to the in-state use or consumption by the purchaser of products from a vendor located outside the state when such purchases are not otherwise subject to tax.<sup>19</sup> In general, the use tax is technically owed by the consumer.<sup>20</sup> But states require vendors to collect the use tax because obtaining the tax from consumers is a difficult administrative chore and consumer self-compliance is notoriously low.<sup>21</sup>

In the years prior to *Bellas Hess*, the Court retreated from its pre-existing dormant Commerce Clause doctrine.<sup>22</sup> That doctrine posited that the states could not impose direct burdens, including taxes, on interstate, as opposed to intrastate, commerce.<sup>23</sup> The Court abandoned this “free market” approach in part because, as the twentieth century progressed, the distinction between interstate and intrastate commerce became difficult to define.<sup>24</sup> The Court also became concerned about arbitrary and inconsistent judicial

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<sup>16</sup> *Id.* at 2099.

<sup>17</sup> *See Quill Corp. v. North Dakota*, 504 U.S. 298, 301 (1992); *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 753, 754 (1967). This Article refers to the issue as addressed by these cases with respect to a state's use tax collection duty, but the same issue can also arise in connection with a state's sales tax collection duty. *See, e.g., Quill*, 504 U.S. at 317. The South Dakota law referenced in *Wayfair* technically imposed sales tax and not use tax because the incidence of the tax—with respect to “goods, wares or merchandise” sold at retail to in-state “consumers or users”—was imposed upon the vendor. *See S.D. CODIFIED LAWS* § 10-45-2 (2016). *See also infra* note 108 and accompanying text.

<sup>18</sup> *See, e.g., Nelson v. Sears Roebuck*, 312 U.S. 359, 361, 363 (1941); *Henneford v. Silas Mason Co.*, 300 U.S. 577, 581 (1937).

<sup>19</sup> *Sears Roebuck*, 312 U.S. at 361–63.

<sup>20</sup> *Id.* at 363.

<sup>21</sup> *See Wayfair*, 138 S. Ct. at 2088. *See also Direct Mktg. Ass'n v. Brohl*, 814 F.3d 1129, 1132 (10th Cir. 2016).

<sup>22</sup> *See Michael T. Fatale, The Evolution of Due Process and State Tax Jurisdiction*, 55 SANTA CLARA L. REV. 565, 573–77 (2015).

<sup>23</sup> *See id.* at 573–75.

<sup>24</sup> *See id.* at 573–76.

applications of these concepts because such rulings had the potential to unjustly infringe upon state sovereignty.<sup>25</sup> The Court was guided by its oft-stated conclusion that it was not the purpose of the Commerce Clause to prevent interstate business from paying its fair share of state tax.<sup>26</sup>

As a consequence of the Court's doctrinal evolution, in the mid-part of the twentieth century, state tax jurisdiction was extended to companies whose only contact with a state was the activity of salespersons. Formerly, such contacts had been deemed "interstate" and therefore not sufficient to create taxing jurisdiction. But in a series of cases, the Court rejected this rule.<sup>27</sup> Eventually, the Court extended the principle that permitted the imposition of state tax based upon the activity of salespersons to circumstances where the representatives were not company employees and were engaged in activities other than actually making sales.<sup>28</sup>

*Bellas Hess* involved a fact pattern that further challenged the Court's doctrinal evolution. In *Bellas Hess*, the out-of-state business was a mail-order vendor that conducted significant business in the state without the use of any sales or other representatives.<sup>29</sup> Although the Court had previously departed from the view that the "interstate" nature of a company's in-state contacts could insulate that company from tax, *Bellas Hess* took a step backwards. The Court held that a state could not impose a use tax collection duty upon a seller whose only connection with customers in a state was through the use of common carriers and the United States mail.<sup>30</sup> *Bellas Hess* justified its conclusion by stating that "it is difficult to conceive of commercial transactions more exclusively interstate in character than the mail-order transactions here involved."<sup>31</sup> The Court also supported its logic by focusing on the particular complexities that relate to the collection of use tax—including the fact that such obligations are imposed not only by states but also by numerous municipalities.<sup>32</sup>

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<sup>25</sup> *See id.* at 575.

<sup>26</sup> *See id.* at 575 & n.64.

<sup>27</sup> *See, e.g.,* *Scripto, Inc. v. Carson*, 362 U.S. 207, 208–09 (1960); *Nw. States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 454 (1959). *See also* *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 321 (1945).

<sup>28</sup> *See, e.g.,* *Tyler Pipe v. Wash. Dep't of Revenue*, 483 U.S. 232, 249–50 (1987).

<sup>29</sup> *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 754, 754–55 (1967).

<sup>30</sup> *Id.* at 758.

<sup>31</sup> *Id.* at 759.

<sup>32</sup> *Id.* at 759–60.



The Court noted that, despite its holding, the domain was one where Congress possessed “the power of regulation and control.”<sup>33</sup>

*Bellas Hess* was a 6-3 decision.<sup>34</sup> Writing for the dissenting Justices, Justice Fortas stated that “[t]here should be no doubt that this large-scale, systematic, continuous solicitation and exploitation of the Illinois consumer market is a sufficient ‘nexus’ to require *Bellas Hess* to collect from Illinois customers and to remit the use tax.”<sup>35</sup> Citing the Court’s prior precedent with respect to sales representatives, the dissent argued in favor of “a sensible, practical conception of the Commerce Clause.”<sup>36</sup> The dissent also argued that where a mail-order vendor’s exploitation of the state’s economic market is pervasive, the case for jurisdiction is just as strong as, or perhaps stronger than, where the out-of-state company is subject to tax through the use of in-state sales representatives.<sup>37</sup> The dissent dismissed the majority’s focus on compliance burdens, noting that this analysis underestimated the capacity of technology to ease those difficulties.<sup>38</sup>

*Quill* involved similar facts to *Bellas Hess*.<sup>39</sup> By the time of *Quill*, the Court’s Commerce Clause doctrine had further evolved, and had specifically concluded, in the case of *Complete Auto Transit v. Brady*,<sup>40</sup> that interstate commerce was not immune from state taxation.<sup>41</sup> That conclusion eradicated the conceptual underpinnings of *Bellas Hess*.<sup>42</sup> The Court’s progression of cases between *Bellas Hess* and *Quill* caused the state of North Dakota to posit in *Quill* that *Bellas Hess* had been effectively overruled.<sup>43</sup>

<sup>33</sup> *Id.* at 760. *Quill* would later question whether this was in fact so, given that *Bellas Hess* was decided on both Commerce Clause and Due Process grounds. See *Quill Corp. v. North Dakota*, 504 U.S. 298, 318 (1992).

<sup>34</sup> See *Bellas Hess*, 386 U.S. at 760 (Fortas, J., dissenting).

<sup>35</sup> *Id.* at 761–62 (Fortas, J., dissenting). Justice Fortas was joined by Justices Black and Douglas. See *id.* at 760.

<sup>36</sup> *Id.* at 764–66 (citing *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960)).

<sup>37</sup> *Id.* at 764–65.

<sup>38</sup> *Id.* at 766.

<sup>39</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298, 301 (1992).

<sup>40</sup> 430 U.S. 274 (1977).

<sup>41</sup> *Id.* at 278–79. In *Goldberg v. Sweet*, the Court noted:

The wavering doctrinal lines of our pre-*Complete Auto* cases reflect the tension between two competing concepts: the view that interstate commerce enjoys a “free trade” immunity from state taxation; and the view that businesses engaged in interstate commerce may be required to pay their own way. *Complete Auto* sought to resolve this tension by specifically rejecting the view that the States cannot tax interstate commerce, while at the same time placing limits on state taxation of interstate commerce.

*Goldberg*, 488 U.S. 252, 259 (1989) (internal citations omitted).

<sup>42</sup> *Quill*, 504 U.S. at 323 (White, J., concurring in part and dissenting in part) (stating that the Court’s subsequent cases “disavowed” the “whole notion” underlying *Bellas Hess* “that interstate commerce is immune from state taxation” (internal citation omitted)).

<sup>43</sup> *Id.* at 301. North Dakota declined to follow *Bellas Hess* because “the tremendous social, economic, commercial, and legal innovations’ of the past quarter-century have

In response, the *Quill* Court stated that it generally agreed with North Dakota's analysis.<sup>44</sup> The Court also recognized that "contemporary Commerce Clause jurisprudence might not dictate the same result [as in *Bellas Hess*] were the issue to arise for the first time today . . ." <sup>45</sup> But the Court nonetheless re-affirmed *Bellas Hess*.<sup>46</sup>

*Quill* not only retained *Bellas Hess*, it also effectively expanded the Court's ruling in that case. *Bellas Hess* concluded that a vendor that limited its contacts with a state to those of mail and common carrier could not be subject to state tax—a rule that was generally limited to a mail-order vendor such as the litigant. *Quill* went further, concluding that an out-of-state business could not be subject to a state's use tax collection duty unless it had an in-state "physical presence."<sup>47</sup> *Quill* was clear that physical presence would not exist if a vendor limited its state contacts to the use of mail and common carriers—hence preserving the *Bellas Hess* rule.<sup>48</sup> But the definition of "physical presence" was otherwise ambiguous, as Justice White noted in his dissent,<sup>49</sup> and as numerous state tax cases later illustrated.<sup>50</sup> The saving grace, if there was one, was that the Court suggested that its rule was limited to the use tax collection duty<sup>51</sup>—something that later state cases would also generally affirm.<sup>52</sup>

*Bellas Hess* had been decided on both Commerce Clause and due process grounds—legal inquiries that the Court concluded were "closely related."<sup>53</sup> *Bellas Hess* stated that, notwithstanding the Court's holding, Congress was free to create jurisdictional standards that would govern the assertion of a state's use tax collection.<sup>54</sup> But *Quill* noted that, despite the Court's prior

rendered its holding 'obsole[te].'" *Id.* (quoting *State v. Quill Corp.*, 470 N.W. 2d 203, 208 (N.D. 1991)). See *State v. Quill*, 470 N.W. 2d at 209–13 (citing Supreme Court cases indicating the change in the "legal landscape").

<sup>44</sup> *Quill*, 504 U.S. at 301–02.

<sup>45</sup> *Id.* at 311.

<sup>46</sup> *Id.* at 301–02.

<sup>47</sup> *Id.* at 317–18. *Bellas Hess* never mentioned the phrase "physical presence." See generally *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 753 (1967).

<sup>48</sup> *Quill*, 504 U.S. at 301.

<sup>49</sup> *Id.* at 337 (White, J., concurring in part and dissenting in part). Justice White's opinion in *Quill* was technically a concurrence in part and a dissent in part because he agreed with the Court's due process analysis. But as Justice White disagreed with the holding and the physical presence rule more generally, this Article will refer to his opinion as a dissent. *Id.*

<sup>50</sup> For cases decided in the immediate aftermath of *Quill*, see Michael T. Fatale, *State Tax Jurisdiction and the Mythical 'Physical Presence' Constitutional Standard*, 54 TAX LAW. 105, 118–30 (2000).

<sup>51</sup> *Quill*, 504 U.S. at 314.

<sup>52</sup> See Fatale, *supra* note 22, at 583–584 n.106.

<sup>53</sup> *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 753, 756 (1967).

<sup>54</sup> *Id.* at 760.

statement, Congress may have felt unable to act, because Congress cannot generally override due process protections.<sup>55</sup> In order to make clear that Congress *could* act, *Quill* justified its re-affirmation of *Bellas Hess* only on Commerce Clause grounds.<sup>56</sup>

*Quill* overruled the component of *Bellas Hess* that determined that a mail-order vendor lacked sufficient due process connections with the state to be subject to tax.<sup>57</sup> The Court in *Quill* noted that when a commercial actor's efforts are "purposefully directed" toward residents of a state, physical contacts are not necessary for an assertion of jurisdiction under the Due Process Clause.<sup>58</sup> The Court observed that the state tax jurisdictional standard resembles that which is applied for purposes of determining adjudicative jurisdiction.<sup>59</sup> It held that this standard was met on the facts since the taxpayer's in-state activity consisted of the "continuous and widespread solicitation of business."<sup>60</sup> The Court noted that when these are the facts, a taxpayer "clearly has 'fair warning that [its] activity may subject [it] to the jurisdiction of a foreign sovereign."<sup>61</sup>

Eight of the nine Justices in *Quill* supported the re-affirmation of *Bellas Hess* on stare decisis grounds. The majority opinion stated that "the *Bellas Hess* rule has engendered substantial reliance and has become part of the basic framework of a sizable industry."<sup>62</sup> It noted also that the "interest in stability and orderly development of the law' that undergirds the doctrine of *stare decisis*, therefore counsels adherence to settled precedent."<sup>63</sup> This analysis helps explain how the majority could state a Commerce Clause rule that it simultaneously suggested was not supported by constitutional principles. But the three-person concurrence could not go so far, and aligned itself with the majority only on stare decisis grounds.<sup>64</sup> *Quill*'s reliance analysis was also predicated, in part, on the conclusion that if the Court overruled *Bellas Hess*, vendors that had relied upon that prior holding could be liable for

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<sup>55</sup> *Quill*, 504 U.S. at 318.

<sup>56</sup> *Id.* at 309–14.

<sup>57</sup> *Id.* at 306–08.

<sup>58</sup> *Id.* at 307–08 (quoting *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985)).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.* at 308.

<sup>61</sup> *Id.* (alterations in original) (quoting *Shaffer v. Heitner*, 433 U.S. 186, 218 (1977) (Stevens, J., concurring)).

<sup>62</sup> *Id.* at 317.

<sup>63</sup> *Id.* (quoting *Runyon v. McCrary*, 427 U.S. 160, 190–91 (1976) (Stevens, J., concurring)).

<sup>64</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2092 (2018) ("Three Justices based their decision to uphold the physical presence rule on *stare decisis* alone." (citing *Quill*, 504 U.S. at 320 (Scalia, J., concurring))). Justice Scalia's concurring opinion in *Quill* was joined by Justices Kennedy and Thomas. *Quill*, 504 U.S. at 320 (Scalia, J., concurring). See also *Quill*, 504 U.S. at 320 (Scalia, J., concurring) ("I would not revisit the merits of [the *Bellas Hess*] holding, but would adhere to it on the basis of *stare decisis*.").

“substantial” retroactive taxes.<sup>65</sup> Justice White stated in his dissent that he believed this concern influenced the Court’s result.<sup>66</sup>

As in *Bellas Hess*, the *Quill* majority supported its constitutional ruling with the further conclusion that the states’ use tax collection laws were burdensome as applied to an out-of-state mail-order vendor.<sup>67</sup> The Court referenced the balancing test applied to state regulations as set forth in the 1970 dormant Commerce Clause case, *Pike v. Bruce Church, Inc.*<sup>68</sup> Under that test, state laws that regulate commercial conduct can be struck down when they are unduly burdensome.<sup>69</sup> But the Court’s analogy seemed inapt, as state taxes are not the equivalents of state regulations—and indeed, as the Court has stated, “are not regulations in any sense of that term.”<sup>70</sup>

Regulations imposed upon commercial conduct are often burdensome because individual states can impose conflicting rules that “materially restrict the free flow of commerce across state lines, or interfere with [such commerce] in matters with respect to which uniformity of regulation is of predominant national concern.”<sup>71</sup> For example, *Quill* cited *Kassel v. Consolidated Freightways Corp.*,<sup>72</sup> where Iowa limited the size of certain trucks to a length that was not common in the adjacent states—a result that caused these trucks to sometimes travel longer distances merely to avoid Iowa.<sup>73</sup> This resulted in private costs that the Court concluded exceeded the benefits to Iowa.<sup>74</sup> A similar pre-*Pike* case is *Southern Pacific Co. v. Arizona*,<sup>75</sup> cited by *Wayfair*, in which an Arizona law prohibited passenger trains with more than fourteen cars and prohibited freight trains with more than seventy cars where 93% to 95% of Arizona train traffic continued outside the state and acceptance of longer train lengths in other states was

<sup>65</sup> *Quill*, 504 U.S. at 317, 318 n.10.

<sup>66</sup> *See id.* at 332 (White, J., concurring in part and dissenting in part).

<sup>67</sup> *See id.* at 314 n.6.

<sup>68</sup> *See id.* at 312. The Court in *Quill* indirectly referenced the balancing test of *Pike v. Bruce Church Inc.*, 397 U.S. 137, 142 (1970), by citing the decision of *Kassel v. Consol. Freightways Corp.*, 450 U.S. 662, 671 (1981), which itself referenced the balancing test set forth in the *Pike* decision. *See Kassel*, 450 U.S. at 670–71.

<sup>69</sup> *See Pike*, 397 U.S. at 142.

<sup>70</sup> *Nw. Portland Cement Co. v. Minnesota*, 358 U.S. 450, 461 (1959).

<sup>71</sup> *S. Pac. Co. v. Arizona*, 325 U.S. 761, 770 (1945). *See* John A. Swain, *State Income Tax Jurisdiction: A Jurisprudential and Policy Perspective*, 45 WM. & MARY L. REV. 319, 340 (2003) (“[R]egulatory burdens cases typically involve a state regulation that is out of sync with neighboring states, or with states nationwide.”).

<sup>72</sup> *Quill*, 504 U.S. at 312.

<sup>73</sup> *Kassel*, 450 U.S. at 665, 674–75.

<sup>74</sup> *See id.* at 671–75, 678–79.

<sup>75</sup> 325 U.S. 761 (1945).

the “standard practice.”<sup>76</sup> Because this was so, *Southern Pacific* concluded that “the state interest is outweighed by the interest of the nation in an adequate, economical and efficient railway transportation service.”<sup>77</sup>

In contrast, the imposition of a state use tax collection duty does not materially restrict the free flow of commerce across state lines.<sup>78</sup> As the Court has repeatedly stated when evaluating state taxes, “businesses engaged in interstate commerce may be required to pay their own way.”<sup>79</sup> Also, while it is hypothetically possible that two states could attempt to apply sales or use tax to the same transaction, credits as applied between the states typically address that concern.<sup>80</sup> Moreover, as a general matter the right of taxation is of greater importance to state sovereignty than the ability to merely regulate commercial conduct, as taxes fund all other state activity.<sup>81</sup>

Recognizing the differences between taxes and regulations, the Court’s Commerce Clause doctrine applies different tests to evaluate the validity of each.<sup>82</sup> By taking *Pike*, a rule that applies to the state regulation of commercial actors and adapting it to the imposition of a state tax, *Quill* stated an exception to these

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<sup>76</sup> See *S. Pac. Co.*, 325 U.S. at 771; see also *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2091 (2018).

<sup>77</sup> *S. Pac. Co.*, 325 U.S. at 783–84.

<sup>78</sup> See *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 364 (1941) (rejecting the taxpayer’s claim that imposition of the state’s use tax collection duty resulted in “an unconstitutional burden on a foreign corporation”); see also *Monamotor Oil Co. v. Johnson*, 292 U.S. 86, 95 (1934) (“The [state] statute obviously was not intended to reach transactions in interstate commerce, but to tax the use of motor fuel after it had come to rest in Iowa, and the requirement that the appellant as the shipper into Iowa shall, as agent of the state, report and pay the tax on the gasoline thus coming into the state for use by others on whom the tax falls imposes no unconstitutional burden either upon interstate commerce or upon the appellant.”).

<sup>79</sup> See *Goldberg v. Sweet*, 488 U.S. 252, 259 (1989) (evaluating a tax imposed on interstate phone calls that the Court equated to a sales tax). See also *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 623–24 (1981) (“[I]t was not the purpose of the [C]ommerce [C]lause to relieve those engaged in interstate commerce from their just share of [the] state tax burden even though it increases the cost of doing business.”) (quoting *Colonial Pipeline Co. v. Traigle*, 421 U.S. 100, 108 (1975) (evaluating the imposition of a use tax)).

<sup>80</sup> See, e.g., *Okla. Tax Comm’n v. Jefferson Lines, Inc.*, 514 U.S. 175, 192–94 (1995); *Regency Transp. v. Comm’r of Revenue*, 42 N.E.3d 1133, 1139–40 (Mass. 2016).

<sup>81</sup> See, e.g., *Arkansas v. Farm Credit Servs. of Cent. Ark.*, 520 U.S. 821, 826 (1997) (“The States’ interest in the integrity of their own processes is of particular moment respecting questions of state taxation. . . . The power to tax is basic to the power of the State to exist.”); see also Michael T. Fatale, *Common Sense: Implicit Constitutional Limitations on Congressional Preemptions of State Tax*, 2012 MICH. ST. L. REV. 41, 42 n.3, 44 (2012) (citing cases and constitutional history); Hayes R. Holderness, *Taking Due Process Seriously: The Give and Take of State Taxation*, 20 FLA. TAX REV. 371, 385 & n.42 (2017) (citing cases).

<sup>82</sup> See Fatale, *supra* note 81, at 60, 63–64 (noting that the Court has applied *Pike* and a second test evaluating whether the state action is discriminatory to regulations, whereas taxes have been evaluated under a four-part test as stated in *Complete Auto Transit v. Brady*, 430 U.S. 274, 278–79 (1977)).

otherwise distinct general rules. *Quill* seemed to defend its logic by suggesting that the use tax collection duty—the collection of tax by an intermediary—is akin to a regulation as opposed to the imposition of a tax.<sup>83</sup> But the Court did so without explaining the break with its pre-existing cases, which were to the contrary.<sup>84</sup> This faulty logic supports the notion that *Quill*'s analysis was more result-driven than doctrinal.<sup>85</sup>

In any event, although *Quill* referenced the *Pike* undue burden test, it did not apply that test—nor did it suggest to lower state courts that they were to apply that test—as the Court's analysis was intended merely to reaffirm the holding in *Bellas Hess* and to posit a physical presence “bright-line” rule.<sup>86</sup> The bright-line rule was to establish a “demarcation of a discrete realm of commercial activity that is free from interstate taxation”<sup>87</sup>—a proposition directly at odds with the thrust of the Court's prior dormant Commerce Clause cases.<sup>88</sup> Therefore, *Quill* invoked *Pike* to support a result that was legally questionable even at the time of the Court's decision.<sup>89</sup>

Although six Justices supported the Court's undue burden reasoning in *Bellas Hess*, only five did so in *Quill*.<sup>90</sup> Justice White in

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<sup>83</sup> See *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992) (noting that the Court had previously ruled that the dormant Commerce Clause “bars state regulations that unduly burden interstate commerce” (emphasis added) (citing *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662 (1981))); see also *Quill*, 504 U.S. at 313 n.6 (referencing the special burdens that result from the use tax collection duty). Cf. *Capital One Bank v. Comm'r of Revenue*, 899 N.E.2d 76, 85 n.17 (Mass. 2009) (noting the special burdens that exist in the use tax collection context as evaluated in *Quill*, as compared to the lesser burdens that result from the imposition of a corporate income tax). See also Swain, *supra* note 71, at 339–43 (evaluating *Quill* as “a regulatory burdens case, not a tax case”).

<sup>84</sup> See, e.g., *Nelson v. Sears Roebuck & Co.*, 312 U.S. 359, 364 (1941) (upholding a use tax collection duty imposed with respect to a vendor's out-of-state mail-order sales as made to in-state consumers; concluding the tax and the related burdens were justified because they pertained to the vendor's privilege of doing business in the state). See generally *Fatale*, *supra* note 81, at 60, 63–64.

<sup>85</sup> See Charles Rothfeld, *Quill: Confusing the Commerce Clause*, 56 TAX NOTES 487, 491–92 (1992) (“[B]y purporting to find value in the ‘undue burdens’ analysis, the Court was able to justify leaving the *Bellas Hess* Commerce Clause holding in place while scrapping a due process ruling that (though no more vulnerable on the merits) stood as an obstacle to action by Congress.”) (concluding that *Quill* was effectively a “political decision” primarily intended to provoke action by Congress); see also Swain, *supra* note 71, at 342 (stating that in seeking to “find a substantive law justification for allowing the doctrine of stare decisis to control the outcome,” *Quill*, in part, “shoehorns its Commerce Clause burden concerns” into the nexus analysis).

<sup>86</sup> *Quill*, 504 U.S. at 305–06, 315, 317.

<sup>87</sup> *Id.* at 314–15.

<sup>88</sup> See *supra* notes 22–28, 41–45 and accompanying text.

<sup>89</sup> See *id.*

<sup>90</sup> See *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 753, 760 (1967) (Fortas, J., dissenting) (joined by Justice Black and Justice Douglas); see also *Quill*, 504 U.S. at 320–21 (Scalia, J., concurring) (joined by Justice Kennedy and Justice Thomas); *id.* at 321–22 (White, J., concurring in part and dissenting in part).



his *Quill* dissent recognized that a taxpayer could be subject to potentially unlawful “multiple tax burdens,”<sup>91</sup> but concluded that there was no such threat on the facts of the case.<sup>92</sup> The *Quill* majority, as noted, specifically punted the entire issue to Congress, and apparently expected that, having done so, Congress would act.<sup>93</sup>

Between *Bellas Hess* and *Quill*, the Court clarified the purpose inherent in its dormant Commerce Clause jurisprudence. In the early twentieth century that purpose was to prevent states from imposing direct burdens on interstate commerce in order to protect free trade.<sup>94</sup> In the latter part of the century the focus shifted to concerns about “economic protectionism” or “regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors.”<sup>95</sup> But with respect to the latter purpose, *Quill* also was out-of-step. The lower North Dakota court, reversed by *Quill*, noted that since “the ‘very object’ of the Commerce Clause is protection of interstate business against discriminatory local practices, it would be ironic to exempt *Quill* from this burden and thereby allow it to enjoy a significant competitive advantage over local retailers.”<sup>96</sup> But of course that is precisely what the *Quill* Court did.<sup>97</sup>

### III. THE SOUTH DAKOTA STATUTE

The South Dakota statute at issue in *Wayfair* had its genesis in a prior action in which the state of Colorado sought to enhance its collection of use tax derived from sales made by out-of-state vendors lacking in-state physical presence.<sup>98</sup> In that circumstance, Colorado required these vendors, sometimes referred to as “remote vendors,” to provide large dollar consumers with year-end statements as to their purchases.<sup>99</sup> Colorado also required these vendors to provide the state’s revenue agency with the purchase information of such large dollar consumers.<sup>100</sup> The general notion was that this notice

<sup>91</sup> See *Quill*, 504 U.S. at 326 (White, J., concurring in part and dissenting in part).

<sup>92</sup> See *id.* at 328 (White, J., concurring in part and dissenting in part).

<sup>93</sup> *Id.* at 318–19.

<sup>94</sup> See *supra* notes 22–24 and accompanying text.

<sup>95</sup> See *Dep’t of Revenue of Ky. v. Davis*, 553 U.S. 328, 337–38 (2008) (stating also, “[t]he modern law of what has come to be called the dormant Commerce Clause is driven by concern about ‘economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors.’”) (quoting *New Energy Co. v. Linbach*, 486 U.S. 269, 273–74 (1988)).

<sup>96</sup> *Quill*, 504 U.S. at 304 n.2 (quoting *State v. Quill Corp.*, 470 N.W.2d 203, 214–15 (N.D. 1991)).

<sup>97</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2094 (2018) (“*Quill* puts both local businesses and many interstate businesses with physical presence at a competitive disadvantage relative to remote sellers.”).

<sup>98</sup> See *State v. Wayfair, Inc.*, 901 N.W.2d 754, 757–58 (S.D. 2017) (citing *Direct Mktg. Ass’n v. Brohl*, 135 S. Ct. 1124, 1135 (2015)).

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

and reporting—similar to what the federal government requires using IRS Form 1099—would tend to increase self-reporting by individual consumers.

Remote vendors that would be subject to the Colorado statute sued to enjoin its enforcement and succeeded in enjoining that statute for six years.<sup>101</sup> Along the way, a dispute arose as to whether the case belonged in federal or state court, and that specific question ascended to the Supreme Court.<sup>102</sup> The Court's unanimous ruling, in *Direct Marketing Ass'n v. Brohl*, was that the case could be tried in federal court.<sup>103</sup> However, the most significant thing about the Court's decision was Justice Kennedy's concurrence. In that concurrence Justice Kennedy departed from the merits of the case to recognize that the Colorado statute was only enacted as a means through which the state could capture use tax revenue that it was proscribed from directly collecting from remote vendors because of *Quill*.<sup>104</sup> Justice Kennedy, who was one of the Justices that previously concurred in *Quill*, stated that it was time for the Court to reconsider that earlier decision.<sup>105</sup>

The South Dakota statute was a response to Justice Kennedy's entreaty in *Direct Marketing Ass'n*.<sup>106</sup> The statute was passed in March of 2016.<sup>107</sup> "The Act provided that any sellers of 'tangible personal property' in South Dakota without a 'physical presence in the state . . . shall remit' sales tax according to the same procedures as sellers with 'a physical presence.'"<sup>108</sup> This collection obligation, however, was limited "to sellers with 'gross revenue' from sales in South Dakota of over \$100,000 per calendar year or with 200 or more 'separate transactions' in the state within the same time frame."<sup>109</sup> The Act included provisions that ensured its immediate application and that enabled the state to bring an expedited declaratory action against vendors that were not in compliance.<sup>110</sup> The Act also included several

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<sup>101</sup> See *Direct Mktg. Ass'n v. Brohl*, 814 F.3d 1129, 1132 (10th Cir. 2016). See also *Direct Marketing Association Reaches Settlement with Colorado*, TAX NOTES: TAX ANALYSTS (Feb. 24, 2017).

<sup>102</sup> *Direct Mktg. Ass'n v. Brohl*, 135 S. Ct. 1124, 1135 (2015).

<sup>103</sup> *Id.* That later federal court case resolved in the State's favor. See *Direct Mktg. Ass'n*, 814 F.3d at 1129. Justice (then-Judge) Gorsuch, who later sided with the State in *Wayfair*, concurred in the court's decision and in so doing criticized *Quill*. *Id.* at 1148–51.

<sup>104</sup> *Direct Mktg. Ass'n*, 135 S. Ct. at 1134–35 (Kennedy, J., concurring).

<sup>105</sup> *Id.*

<sup>106</sup> See *State v. Wayfair*, 901 N.W.2d 754, 757–58 (S.D. 2017).

<sup>107</sup> *Id.* at 759 (citing S. 106, 2016 Legis. Assemb., 91st Sess. (S.D. 2016)).

<sup>108</sup> *Id.* at 758 (citing S.D. S. 106 § 1).

<sup>109</sup> *Id.* (citing S.D. S. 106 §§ 1–2).

<sup>110</sup> *Id.* (citing S.D. S. 106 §§ 2–3).



provisions that enjoined its enforcement while litigation was ongoing and that precluded retroactive enforcement.<sup>111</sup>

Litigation concerning the Act commenced in April of 2016.<sup>112</sup> There were three vendors that took part in the litigation and the limited factual record was the same for each.<sup>113</sup> Those facts, which were agreed to by the parties, were that each seller lacked a physical presence in South Dakota; each met the sales and transaction requirements for application of the Act; and no seller was registered to collect South Dakota sales tax.<sup>114</sup> Because the Act did not require physical presence for the assertion of nexus, the State conceded that its statute was unconstitutional under *Quill*.<sup>115</sup> Therefore, the State quickly lost two cases at the South Dakota circuit court and supreme court—the result that it wanted.<sup>116</sup> The State then filed a petition for review with the United States Supreme Court.<sup>117</sup>

The Court took the case and rendered its decision in June of 2018. The posture of the case—featuring a skeletal factual record and two parties that agreed with the legal analysis of the lower courts—was certainly unusual. And the speed with which the case got to the Court—a little over two years from the time that the state statute to be construed was enacted—was lightning fast. But as Justice Kennedy had previously stated in his *Direct Marketing Ass'n* concurrence, and the state legislation repeated in its justification for the law, the significance of the issue to a state was substantial.<sup>118</sup> And as later noted in Justice Kennedy's opinion in *Wayfair*, the Court had a special rationale for taking the case, as *Quill* represented a “false constitutional premise of the Court's own creation.”<sup>119</sup>

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<sup>111</sup> *Id.* (citing S.D. S. 106 §§ 3, 5–6).

<sup>112</sup> *Id.* at 759.

<sup>113</sup> *Id.*

<sup>114</sup> *Id.* at 759–60.

<sup>115</sup> *Id.* at 760.

<sup>116</sup> *See id.* at 760–61 (referencing the lower court's decision “based on undisputed statements of material fact and the parties' briefs” and also noting the state supreme court's affirmation of that lower court decision). During the litigation, the State also succeeded in contesting the taxpayers' attempt to move the case to federal court. *See generally* South Dakota v. Wayfair, Inc., 229 F. Supp. 3d 1026 (D.S.D. 2017).

<sup>117</sup> Petition for Writ of Certiorari at 12, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494), 2017 WL 4404984 \*12.

<sup>118</sup> Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1134–35 (2015) (Kennedy, J., concurring); *Wayfair*, 901 N.W. 2d at 765–67 (quoting S.B. 106 §§ 8-9, 2016 Legis. Assemb., 91st Sess. (S.D. 2016)).

<sup>119</sup> South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2096 (2018).

## IV. THE WAYFAIR ANALYSIS

Some aspects of the *Wayfair* decision are less than clear because the result was 5-4 and the two concurring Justices clearly disagreed with the three other Justices in the majority on certain issues. The analysis below probes the decision, including the differences among the Justices.

## A. Physical Presence and State Sovereignty

One thing that was clear in *Wayfair* was the Court's ultimate conclusion pertaining to its prior construction of the dormant Commerce Clause. The Court concluded that the "[t]he physical presence rule of *Quill* is unsound and incorrect," and that *Quill* and *Bellas Hess* "should be, and now are, overruled."<sup>120</sup> Both cases needed to be overruled because, although the physical presence rule was only specifically stated in *Quill*, the rule was a general re-affirmation of the logic in *Bellas Hess*.<sup>121</sup> The Court stated that *Quill* was "wrong on its own terms when it was decided in 1992" and "since then the Internet revolution has made its earlier error all the more egregious and harmful."<sup>122</sup>

The Court's holding was by a 5-4 vote, but there was no question concerning the antipathy of all nine Justices to the pre-existing physical presence rule. Within the majority, Justice Thomas stated in concurrence that *Bellas Hess* and *Quill* "can no longer be rationally justified,"<sup>123</sup> and Justice Gorsuch noted in concurrence that *Bellas Hess* and *Quill* were a "mistake."<sup>124</sup> Justice Thomas went so far as to state that he should have joined Justice White's dissent in *Quill*, which was harshly critical of the *Quill* physical presence rule,<sup>125</sup> and Justice Gorsuch similarly cited the White dissent favorably.<sup>126</sup> Even Chief Justice Roberts' four-person dissenting opinion concluded that, although he would have retained the physical presence rule on stare decisis grounds, "*Bellas Hess* was wrongly decided."<sup>127</sup> Underlying all of these statements was the notion that *Bellas Hess* and *Quill* were

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<sup>120</sup> *Id.* at 2099.

<sup>121</sup> *See id.* at 2091–92.

<sup>122</sup> *Id.* at 2097.

<sup>123</sup> *Id.* at 2100 (Thomas, J., concurring) (quoting *Quill Corp. v. North Dakota*, 504 U.S. 298, 333 (1992) (White, J., concurring in part and dissenting in part)).

<sup>124</sup> *Id.* (Gorsuch, J., concurring).

<sup>125</sup> *Id.* (Thomas, J., concurring) (citing *Quill*, 504 U.S. at 322 (White, J., concurring in part and dissenting in part)).

<sup>126</sup> *Id.* (Gorsuch, J., concurring) (citing *Quill*, 504 U.S. at 329 (White, J., concurring in part and dissenting in part)).

<sup>127</sup> *Id.* at 2101 (Roberts, C.J., dissenting). Presumably, Chief Justice Roberts could not call *Quill* a mistake, given the prior decision in *Bellas Hess* that *Quill* re-affirmed, invoking stare decisis, and his later vote for stare decisis in *Wayfair*. *See id.*

mistaken specifically because the cases retained vestiges of the Court's pre-existing "free trade" doctrine.<sup>128</sup>

*Wayfair's* rejection of the physical presence rule as a dormant Commerce Clause requirement also finally resolved, implicitly and without fanfare, the question of whether physical presence was required in any other state tax context—including in particular for purposes of state corporate income tax.<sup>129</sup> Although the physical presence rule as established by *Quill* was limited to the states' use tax collection duty, numerous taxpayers and practitioners claimed in the aftermath of the case that the rule also applied in the corporate income tax area.<sup>130</sup> The state cases that evaluated this question almost invariably ruled that it did not—and most of these cases were denied certiorari by the Supreme Court.<sup>131</sup> But taxpayers and practitioners continued to claim that the issue remained unresolved, arguing that the precedential value of the state cases was limited to their jurisdictions, and to their facts.<sup>132</sup> Taxpayers and practitioners generally claimed that only a Supreme Court decision could finally resolve the question. *Wayfair's* unanimous denunciation of the physical presence rule finally accomplished that resolution.

Another clear aspect of the *Wayfair* decision was the Court's determination that the physical presence rule is in conflict with principles of state sovereignty. The Court noted "the necessity of allowing the States the power to enact laws to implement the political will of their people."<sup>133</sup> It stated that "[t]he physical presence rule . . . is not just a technical legal problem—it is an extraordinary imposition by the Judiciary on the States' authority to collect taxes and perform critical public functions."<sup>134</sup> The Court stated that, "[i]f it becomes apparent that the Court's Commerce Clause decisions prohibit the States from exercising their lawful sovereign powers in our federal system, the Court should be vigilant in correcting the error."<sup>135</sup> Justices Thomas

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<sup>128</sup> See *Quill*, 504 U.S. at 322–24 (White, J., concurring in part and dissenting in part); see also *supra* notes 22–46 and accompanying text.

<sup>129</sup> See, e.g., Andrea Muse, *Wells Fargo Adjusts Income Tax Reserves Following Wayfair*, TAX NOTES (July 23, 2018), <https://www.taxnotes.com/editors-pick/wells-fargo-adjusts-income-tax-reserves-following-wayfair> [<http://perma.cc/AR3R-RT8A>].

<sup>130</sup> See Fatale, *supra* note 50, at 130–41; Fatale, *supra* note 22, at 583–84 n.106.

<sup>131</sup> See Fatale, *supra* note 22, at 583–84 n.106.

<sup>132</sup> See, e.g., Reply Brief Amicus Curiae of the Council on State Taxation in Support of Appellant at 11–12, *Crutchfield Corp. v. Testa*, 88 N.E.3d 900 (Ohio 2016) (No. 15-0386).

<sup>133</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2090 (2018).

<sup>134</sup> *Id.* at 2095.

<sup>135</sup> *Id.* at 2096. Similarly, the Court acknowledged that there could be legal questions about state implementation of its decision but stated that prospect "cannot justify retaining [an] . . . anachronistic rule that deprives States of vast revenues from major businesses." *Id.* at 2099.

and Gorsuch in their concurring opinions were not as explicit in revering state sovereignty, but both made clear that they do not accept the full breadth of the Court's dormant Commerce Clause jurisprudence, because pursuant to that case law "courts may invalidate state laws that offend no congressional statute."<sup>136</sup> Antipathy to the dormant Commerce Clause is effectively an endorsement of state sovereignty because the doctrine imposes significant limitations upon the states' sovereign rights.<sup>137</sup>

One of the more significant questions posed at the *Wayfair* oral argument and in the parties' briefs was whether the striking of the physical presence rule would be retroactive in its effect.<sup>138</sup> It had been widely thought after *Quill* that a primary reason that North Dakota lost that case was because the State's attorney told the Court that, if the State won, it would seek retroactive taxes.<sup>139</sup> In *Wayfair*, the State of South Dakota and the states that joined South Dakota as amici knew that the Court would be concerned with this issue and attempted to address it.<sup>140</sup> But it was nonetheless generally assumed by the parties that if *Wayfair* overturned *Quill*, the ruling would be retroactive.<sup>141</sup> *Wayfair* fulfilled this expectation.<sup>142</sup> The Court did not declare an

<sup>136</sup> *Id.* at 2100 (Gorsuch, J., concurring) (emphasis in original). Justice Thomas stated more generally, similar to his numerous prior statements (see, e.g., *McBurney v. Young*, 569 U.S. 221, 237 (2013)), that the Court's entire dormant Commerce Clause jurisprudence "can no longer be rationally justified." *Id.* (Thomas, J., concurring) (quoting *Quill Corp. v. North Dakota*, 504 U.S. 298, 333 (1992) (White, J., concurring in part and dissenting in part). See also *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 610 (1997) (Thomas, J., dissenting) (noting that the dormant Commerce Clause is "unmoored from any constitutional text" and has resulted in court decisions evaluating "state action far afield from the discriminatory taxes it was primarily designed to check").

<sup>137</sup> See, e.g., *Fatale*, *supra* note 81, at 55–66.

<sup>138</sup> See generally Transcript of Oral Argument, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494), 2018 WL 1811984 (the Court refers to retroactivity four times); see also Petitioner's Brief at 48–51, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494); Respondents' Brief at 62–65, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494).

<sup>139</sup> See Billy Hamilton, *Remembrance of Things Not So Past: The Story Behind the Quill Decision*, 59 ST. TAX NOTES MAG. 807, 809–10 (2011); *Fatale*, *supra* note 81, at 86 & n.267.

<sup>140</sup> See Petitioner's Brief, *supra* note 138, at 48–51; Brief For Colorado and 40 Other States, Two United States Territories, and the District of Columbia as Amici Curiae Supporting Petitioner at 18–21, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494).

<sup>141</sup> See Respondents' Brief, *supra* note 138, at 62; see also Transcript Oral Argument, *supra* note 138, at 51 ("[T]his Court has indicated that a purely prospective ruling is inconsistent with its view of the law and made that very clear in the—*in the Harper case.*") (statement of the attorney for the respondent, *Wayfair*, referencing *Harper v. Va. Dep't of Taxation*, 509 U.S. 86 (1993)). *Quill* of course also assumed that a decision for the State would have been retroactive—which may have influenced the Court in finding against the State of North Dakota. See *supra* notes 65–66 and accompanying text.

<sup>142</sup> The Court noted repeatedly that there would be no retroactivity with respect to the South Dakota law in question because the law itself—and not the Court's construction of the Constitution—foreclosed this possibility. See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2089, 2098 (2018). The Court also noted that if a state sought to apply a similar

exception to the general jurisprudential rule that its constitutional holdings are given retroactive effect.<sup>143</sup> Rather, it made clear that, post-*Wayfair*, the physical presence rule would not apply to prior tax periods.<sup>144</sup> Instead, the Court suggested that retroactive assertions of tax jurisdiction could potentially raise other constitutional issues.<sup>145</sup>

## B. Discrimination and Double Taxation

*Wayfair* is consistent with the Court's modern Commerce Clause precedent in that it posits that the purpose of the Commerce Clause is to prevent "economic discrimination."<sup>146</sup> In contrast, *Quill* was problematic because it created "market distortions" and "artificial competitive advantages."<sup>147</sup> Post-*Wayfair*, the discrimination principle will not typically have any application to the imposition of a state's use tax collection duty since the effect of that imposition is merely to place in-state and out-of-state vendors on equal footing.<sup>148</sup> *Wayfair* seemingly acknowledged this consequence when it stated that "[c]omplex state tax systems could have the effect of discriminating against interstate commerce" but that, of relevance, "in-state businesses pay the taxes as well."<sup>149</sup>

*Wayfair* also suggested state laws that are not uniform could have the effect of discriminating against interstate commerce—which, the Court noted, state membership in the Streamlined Sales and Use Tax Agreement (SSUTA) would help to address.<sup>150</sup> The Court's cryptic reasoning, however, is logical only if one assumes that the application of these "complex state

statute retroactively in a case where consumers had already self-reported the tax, the state could potentially be accused of imposing an unlawful double tax. *Id.* at 2099. These issues, the Court stated, "are not before the Court in the instant case; but their potential to arise in some later case cannot justify retaining this artificial, anachronistic rule that deprives States of vast revenues from major businesses." *Id.*

<sup>143</sup> See *Harper v. Va. Dep't of Taxation*, 509 U.S. 86, 90 (1993).

<sup>144</sup> The Court noted the prospect that the decision could have retroactive effect pursuant to the law of a state other than South Dakota, where the state statute itself foreclosed this possibility. *Wayfair*, 138 S. Ct. at 2098–99. The Court concluded that such treatment in another state was an issue for a later day. *Id.* at 2099.

<sup>145</sup> See *Wayfair*, 138 S. Ct. at 2099. For example, there could be a retroactivity issue arising under the Due Process Clause. See *infra* notes 200–202 and accompanying text.

<sup>146</sup> 138 S. Ct. at 2093–94; see also *supra* note 95 and accompanying text.

<sup>147</sup> 138 S. Ct. at 2092, 2094.

<sup>148</sup> See *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 364–65 (1941) ("A tax or other burden obviously does not discriminate against interstate commerce where 'equality is its theme.'") (citing *Henneford v. Silas Mason Co.*, 300 U.S. 577, 583–586 (1937); *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 48–49 (1940); see also *Wayfair*, 138 S. Ct. at 2094, 2096 (noting that the Commerce Clause was intended to put in-state and out-of-state commercial actors on an "even playing field" and that the *Quill* physical presence rule was inconsistent with that goal).

<sup>149</sup> *Wayfair*, 138 S. Ct. at 2099.

<sup>150</sup> *Id.* at 2099–100.

tax systems” could somehow result in an impermissible double tax—perhaps by enabling a state to claim a taxable sale that logically belongs to a second state.<sup>151</sup> Such a consequence would be somewhat reminiscent of the Court’s recent decision in *Comptroller of the Treasury v. Wynne*.<sup>152</sup> Although *Wynne* is not referenced in the *Wayfair* majority opinion, it may have influenced the Court’s reasoning.<sup>153</sup> But such double taxation under the state’s sales tax laws is unusual and, in any event, is generally addressed, when it occurs, through the conferral of a state tax credit.<sup>154</sup>

The Court also made the peculiar statement that:

Others [i.e., certain non-litigant interested parties] have argued that retroactive liability risks a double tax burden in violation of the Court’s apportionment jurisprudence because it would make both the buyer and the seller legally liable for collecting and remitting the tax on a transaction intended to be taxed only once.<sup>155</sup>

The Court’s suggestion is that if a state required a vendor to collect use tax on a retroactive basis, it could effectively be imposing double tax because the consumer might have already independently submitted the tax. This statement is peculiar in part because it is attributed not to the Court’s own logic, but to persons that were not litigants in the case. Also—perhaps explaining the Court’s ambivalence—double taxation does not necessarily result in a constitutional infringement.<sup>156</sup> Further, as the Court noted, one of the difficulties that the states faced when applying the *Quill* physical presence rule was that very few consumers independently submit use tax.<sup>157</sup>

<sup>151</sup> *Id.* at 2099. The Streamlined Sales Tax Governing Board filed an amicus brief in the *Wayfair* case that referenced the various ways in which SSUTA helps make state laws uniform. See generally Brief for Amicus Curiae Streamlined Sales Tax Governing Board, Inc. In Support of Petitioner, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494). That brief did not make any claim that SSUTA serves to address state tax discrimination—and in fact never mentions “discrimination”—but did state that SSUTA includes “uniform sourcing rules to prevent double taxation.” See *id.* at 14.

<sup>152</sup> 135 S. Ct. 1787, 1801–06 (2015) (pertaining to a state personal income tax).

<sup>153</sup> *Wynne*, like *Wayfair*, was a 5-4 decision. See *id.* at 1791. Justice Alito was the author of *Wynne*. *Id.* It was commonly thought after the *Wayfair* hearing that South Dakota had four votes—Justices Kennedy, Thomas, Gorsuch, and Ginsburg—but not necessarily a fifth. See, e.g., Michael Cullers, *Oyez! The Supreme Court Hears Oral Arguments in Wayfair, and Now We Play the Waiting Game*, PUB. FIN. L. BLOG (Apr. 26, 2008), <https://www.publicfinancetaxblog.com/2018/04/oyez-the-supreme-court-hears-oral-arguments-in-wayfair-and-now-we-play-the-waiting-game/> [http://perma.cc/3RW4-K4FP]. It seems fair to speculate that the Court’s double tax verbiage was what helped to secure Justice Alito’s deciding vote.

<sup>154</sup> See *Okla. Tax Comm’n v. Jefferson Lines, Inc.*, 514 U.S. 175, 194–95 (1995).

<sup>155</sup> *Wayfair*, 138 S. Ct. at 2099 (citing Brief of Amici Curiae Law Professors and Economists in Support of Petitioner, at 7, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (No. 17-494)).

<sup>156</sup> See, e.g., *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 170–71 (1983).

<sup>157</sup> See *Wayfair*, 138 S. Ct. at 2088; see also *Direct Mktg. Ass’n v. Brohl*, 135 S. Ct. 1124, 1135 (2015) (Kennedy, J., concurring) (citing CALIFORNIA STATE BOARD OF EQUALIZATION,



## C. Due Process

### 1. The Nexus Implications of *Wayfair*

Implicitly, when *Wayfair* conceded that the physical presence rule derived from *Bellas Hess* and *Quill* was incorrect, it re-posed that the relevant nexus considerations are based in due process. This is because both *Bellas Hess* and *Quill* recognized that absent the notion of physical presence, the jurisdictional rules are primarily those of due process.<sup>158</sup>

The Court's analysis of Due Process Clause and Commerce Clause nexus in *Bellas Hess* and *Quill* was intertwined such that *Wayfair* felt obliged to overrule both cases in their entirety, but the Court was nonetheless clear that it was only the physical presence rule that it rejected.<sup>159</sup> Moreover, in the absence of *Bellas Hess* and *Quill*, constitutional nexus must be derivative of due process principles, since this was clearly the law prior to *Bellas Hess*, and was generally the law even between those two cases.<sup>160</sup> The majority decision in *Wayfair* heavily relied upon Justice White's dissent in *Quill*.<sup>161</sup> Moreover, Justices Thomas and Gorsuch in their concurrences both specifically aligned themselves

REVENUE ESTIMATE: ELECTRONIC COMMERCE AND MAIL ORDER SALES, REV. 8/13, at 7 (2013), <https://www.boe.ca.gov/legdiv/pdf/e-commerce-08-21-13F.pdf> [<http://perma.cc/TGR6-QP2L>] (estimating the rate of compliance at 4%).

<sup>158</sup> See *supra* notes 53–56 and accompanying text. See also *Quill Corp. v. North Dakota*, 504 U.S. 298, 325–27 (1992) (White, J., concurring in part and dissenting in part) (stating, *inter alia*, that the Court has “never . . . found . . . sufficient contacts for due process purposes but an insufficient nexus under the Commerce Clause” and that *Complete Auto* makes clear that the Court's nexus requirement is traceable to concerns “grounded in the Due Process Clause”); Rothfeld, *supra* note 85, at 488 (noting that the Court's Commerce Clause nexus rule prior to *Quill* was “borrowed wholesale from decisions involving the Due Process Clause”).

<sup>159</sup> *Wayfair*, 138 S. Ct. at 2093 (“Physical presence is not necessary to create a substantial nexus.”); *id.* at 2099 (“[T]he physical presence rule of *Quill* is unsound and incorrect.”). Hence, *Wayfair* cites favorably both *Bellas Hess* and *Quill* in its due process analysis. See *id.* at 2093.

<sup>160</sup> *Quill*, 504 U.S. at 325–27 (White, J., concurring in part and dissenting in part) (stating, *inter alia*, that when the Court announced its decision in the 1977 case, *Complete Auto*, “the nexus requirement was definitely traceable to concerns grounded in the Due Process Clause”); see also *Trinova Corp. v. Mich. Dep't of Treasury*, 498 U.S. 358, 373 (1991) (the four tests set forth in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), including the nexus test, “while responsive to Commerce Clause dictates, encompass[s] as well the due process requirement that there be a ‘minimal connection’ between the interstate activities and the taxing State, and a rational relationship between the income attributed to the State and the intrastate values of the enterprise”); *Quill*, 504 U.S. at 314 (acknowledging the Court's retreat between *Bellas Hess* and *Quill* “from the formalistic constrictions of a stringent physical presence test in favor of a more flexible substantive approach” (internal citation omitted)).

<sup>161</sup> The Court referred favorably to Justice White's dissent four times. See *Wayfair*, 138 S. Ct. at 2092, 2094, 2096–97.



with White's dissent.<sup>162</sup> In that dissent, Justice White specifically stated that nexus is primarily a due process inquiry.<sup>163</sup>

The context in which *Wayfair* was decided also supports the conclusion that the state tax nexus inquiry is now generally a due process test. Subsequent to *Quill*, most state courts that considered the issue eventually concluded that the physical presence rule did not apply to other state taxes, and in particular to the corporate income tax.<sup>164</sup> In that context, these courts generally determined nexus by relying upon due process principles.<sup>165</sup> At the *Wayfair* hearing, the point was made that dispensing with the physical presence rule would not be problematic specifically because there has been little difficulty in applying the nexus analysis in these other state court cases.<sup>166</sup> The *Wayfair* majority seemed to accept that argument.

## 2. The Substance of the Nexus Test

Although its analysis was brief, *Wayfair* also made clear the substance of the due process inquiry.<sup>167</sup> The Court cited *Bellas Hess* for the proposition that the Commerce Clause "nexus requirement is 'closely related' to the due process requirement that there be 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.'"<sup>168</sup> Also, the Court stated that although in the tax area Due Process and Commerce Clause nexus standards "may not be identical or conterminous . . . there are significant parallels."<sup>169</sup>

*Quill* had noted that the rules that apply for purposes of due process nexus are similar to those that apply for purposes of adjudicative jurisdiction.<sup>170</sup> *Wayfair* is consistent with this conclusion because it cites favorably both *Quill* and *Burger King Corp. v. Rudzewicz*,<sup>171</sup> an adjudicative jurisdiction case, when

<sup>162</sup> *Id.* at 2100 (Thomas, J., concurring); *id.* (Gorsuch, J., concurring).

<sup>163</sup> *See Quill*, 504 U.S. 325–27 (White, J., concurring in part and dissenting in part). The four-person *Wayfair* dissent may also have generally accepted the *Quill* reasoning of Justice White, consistent with the analysis in the *Wayfair* majority opinion. *See Wayfair*, 138 S. Ct. at 2010 (Roberts, C.J., dissenting) ("I agree that *Bellas Hess* was wrongly decided, for many of the reasons given by the Court.").

<sup>164</sup> *See Fatale, supra* note 22, at 583–84 n.106.

<sup>165</sup> *See id.* at 583–85.

<sup>166</sup> Transcript of Oral Argument, *supra* note 138, at 4–5, 56–57.

<sup>167</sup> *Wayfair*, 138 S. Ct. at 2093.

<sup>168</sup> *Id.* at 2093 (citing *Nat'l Bellas Hess v. Dep't of Revenue*, 386 U.S. 753, 756 (1967) and *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344–45 (1954)).

<sup>169</sup> *Id.*

<sup>170</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298, 307–08 (1992). *See also id.* at 319 (Scalia, J., concurring) ("It is difficult to discern any principled basis for distinguishing between jurisdiction to regulate and jurisdiction to tax.").

<sup>171</sup> 471 U.S. 462 (1985).

evaluating due process nexus.<sup>172</sup> As stated by *Quill*, the Court has often identified “‘notice’ or ‘fair warning’ as the analytic touchstone of due process nexus analysis.”<sup>173</sup> This standard is satisfied where a commercial actor’s efforts are “purposefully directed” toward the residents of a state.<sup>174</sup> For example, in *Wayfair*, the nexus standard was met where the respondents had sufficient “economic and virtual contacts . . . with the State.”<sup>175</sup> Further, the Court’s precedents make clear that this standard can be satisfied by either direct or indirect contacts—for example, contacts that are effected through an intermediary.<sup>176</sup> Although physical presence is no longer necessary to establish nexus, it is sufficient to create nexus, whether or not that presence relates to the company’s in-state sales.<sup>177</sup>

*Wayfair* specifically concluded that the Commerce Clause “substantial nexus” requirement is met “when the taxpayer [or collector] ‘avails itself of the substantial privilege of carrying on business’ in that jurisdiction.”<sup>178</sup> For this proposition, the Court quoted *Polar Tankers, Inc. v. City of Valdez*.<sup>179</sup> But, as *Polar Tankers* makes clear, this standard ultimately derives from the due process analysis in *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*.<sup>180</sup> It might seem odd at first blush that the Court’s

<sup>172</sup> See *Wayfair*, 138 S. Ct. at 2093 (citing *Quill*, 504 U.S. at 308 and *Burger King Corp.*, 471 U.S. at 476).

<sup>173</sup> *Quill*, 504 U.S. at 312 (stating also, “[d]ue process centrally concerns the fundamental fairness of governmental activity”).

<sup>174</sup> See *id.* at 307–08; see also *J. McIntyre Machinery, Ltd. v. Nicastro*, 564 U.S. 873, 877 (2011).

<sup>175</sup> *Wayfair*, 138 S. Ct. at 2099.

<sup>176</sup> See *Fatale*, *supra* note 22, at 619–21 (discussing *J. McIntyre Machinery*, 564 U.S. 873 and *Asahi Indus. Co. v. Superior Court of Calif.*, 480 U.S. 102 (1987)).

<sup>177</sup> See *Wayfair*, 138 S. Ct. at 2093 (“Physical presence is *not necessary* to create a substantial nexus.”) (emphasis added); see also *Quill*, 504 U.S. at 330 (White, J., concurring in part, dissenting in part) (noting that under the Court’s pre-*Quill* precedent, for example, *Nat’l Geographic Soc’y v. Cal. Bd. of Equalization*, 430 U.S. 551, 560–62 (1977), mail-order sellers are subject to use tax collection when “they have some presence in the taxing state even if that activity has no relation to the transaction being taxed”). *Nat’l Geographic* was cited favorably by *Wayfair*. See 138 S. Ct. at 2098, 2094. Cf. *Crutchfield Corp. v. Testa*, 88 N.E.3d 900, 912–13 (Ohio 2016) (concluding that physical presence is a sufficient but not necessary condition for applying a state corporate gross receipts tax).

<sup>178</sup> *Wayfair*, 138 S. Ct. at 2099 (quoting *Polar Tankers, Inc. v. City of Valdez*, 557 U.S. 1, 11 (2009)).

<sup>179</sup> 557 U.S. 1 (2009) (case pertaining to a city’s personal property tax imposed upon the value of large ships traveling to and from such city).

<sup>180</sup> *Id.* at 11 (citing *Mobil Oil Corp. v. Comm’r of Taxes of Vt.*, 445 U.S. 425, 437 (1980)). The analysis in *Mobil Oil*, in turn, derived from the Court’s due process holding in *Wisconsin v. J.C. Penney*, 311 U.S. 435, 444–45 (1940). See *Mobil Oil*, 445 U.S. at 437 (citing to *J.C. Penney Co.*, 311 U.S. 435, 444–45); *J.C. Penney Co.*, 311 U.S. at 444–45 (stating that when evaluating due process as applied to the imposition of a state tax “[t]he simple but controlling question is whether the state has given anything for which it can ask return”); see also *Holderness*, *supra* note 81, at 381–84 (discussing the due process test stated by *J.C. Penney Co.*).

important re-affirmation of the purposeful availment principle relies on language in a somewhat aberrational case focused on one of the Constitution's least-known provisions, the so-called "Tonnage Clause."<sup>181</sup> But the Court obviously sought to cite a post-*Quill* precedent, and it had not taken any nexus cases subsequent to *Quill*.<sup>182</sup>

### 3. Nexus in Application

*Wayfair* evaluated how the nexus analysis would apply to facts like those at issue and to the specific facts in question. Specifically, the Court noted that the South Dakota Act only applied to sellers that delivered more than \$100,000 of goods or services into South Dakota or engaged in 200 or more separate transactions for the delivery of goods into the state on an annual basis.<sup>183</sup> It stated that "[t]his quantity of business could not have occurred unless the seller availed itself of the substantial privilege of carrying on business in South Dakota."<sup>184</sup> The Court allowed for the prospect that in the abstract some remote vendors could have only "*de minimis* contacts" with the state, but the Court's analysis seems to foreclose this possibility in any case where the South Dakota thresholds are met.<sup>185</sup>

More generally, *Wayfair* implicitly concluded that the nexus requirement for use tax collection would be satisfied in any state where a vendor exceeded nexus thresholds substantially identical to those of South Dakota.<sup>186</sup> By way of comparison, in the corporate income tax area, the states have utilized different sales thresholds for asserting "factor presence" economic nexus, and such thresholds are sometimes higher in high-population states.<sup>187</sup> But *Wayfair* does

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<sup>181</sup> See *Polar Tankers*, 557 U.S. at 4–5.

<sup>182</sup> See *Wayfair*, 138 S. Ct. at 2099 (citing *Polar Tankers* with respect to the rule as to substantial nexus "[i]n the absence of *Quill* and *Bellas Hess*"). Cf. *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16, 24–25 (2008) ("The 'broad inquiry' subsumed in [the Commerce Clause and due process] constitutional requirements [in state tax matters] is 'whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state'—that is, 'whether the state has given anything for which it can ask return.'") (quoting *ASARCO Inc. v. Idaho Tax Comm'n*, 458 U.S. 307, 315 (1982), in turn quoting *J.C. Penney Co.*, 311 U.S. at 444).

<sup>183</sup> *Id.* at 2099 (citing S.B. 106 § 1, 2016 Leg., Gen. Sess. (S.D. 2016)).

<sup>184</sup> *Id.*

<sup>185</sup> See *id.*; see also *id.* at 2098–99 (noting that "[t]he law at issue requires a merchant to collect the tax only if it does a considerable amount of business in the State" and that the law "applies a safe harbor to those who transact only limited business" in the state).

<sup>186</sup> See *id.* at 2099. Cf. *Quill Corp. v. North Dakota*, 504 U.S. 296, 308 (1992) (holding that when a corporation engages in "continuous and widespread solicitation of business within a State. . . [s]uch a corporation clearly has 'fair warning that [its] activity may subject [it] to the jurisdiction of a foreign sovereign'" (citing *Shaffer v. Heitner*, 433 U.S. 186, 218 (1977) (Stevens, J., concurring))).

<sup>187</sup> See, e.g., *The State Income Tax Consequences of Wayfair*, BDO (Aug. 2018), <https://www.bdo.com/insights/tax/state-and-local-tax/the-state-income-tax-consequences->

not suggest that the jurisdictional thresholds to be used for purposes of the states' use tax collection duties must be based upon a state's population. *Wayfair* concluded that the thresholds used by South Dakota, a small population state, pertained to companies whose business in the state was "substantial"—a concept that the Court evaluated in the abstract.<sup>188</sup> In the case briefs and at oral argument, questions were raised about whether it would be appropriate for a state to assert jurisdiction over a vendor making only a single sale into the state where presumably that sale exceeded the state's \$100,000 threshold<sup>189</sup> or, alternatively, over a vendor making 200 sales where each of those individual sales were a very low dollar amount (say \$2).<sup>190</sup> But *Wayfair* suggests no constitutional concern with either fact pattern.

As noted, *Quill* stated that the due process tax jurisdiction rules generally track the standards applied to determine adjudicative jurisdiction.<sup>191</sup> In that latter context, there have been cases in recent years questioning whether a single sale made with respect to a state would suffice.<sup>192</sup> But the Court has also stated—as *Wayfair* itself did—that the state tax jurisdiction and adjudicative jurisdiction standards are not identical.<sup>193</sup> To the extent that there are differences, the Court has inferred that it is the adjudicative jurisdiction principles that are more rigorous.<sup>194</sup> Because *Wayfair* expressed no specific concern with the assertion of state tax jurisdiction when a taxpayer makes only a single large-dollar sale into a state—unlike in the Court's recent adjudicative jurisdiction cases—it generally supports that point.

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of-wayfair [<http://perma.cc/D9UG-NLX3>] (noting factor-presence corporate income tax statutes in New York, Ohio, Michigan, and Washington that originally asserted nexus based on in-state sales of \$1,000,000, \$500,000, \$350,000, and \$250,000, respectively).

<sup>188</sup> *Wayfair*, 138 S. Ct. at 2099. See also *supra* notes 183–185 and accompanying text. Similarly, a recent congressional bill that would have addressed *Quill*, which passed the Senate but not the House, would have required a remote Internet vendor to collect use tax in every state where such vendor had more than \$1 million in total Internet sales—irrespective of its sales volume in any particular state. See also Fatale, *supra* note 22, at 633–36 (discussing the Marketplace Fairness Act, S. 336, S. 743, H.R. 684 113th Cong. (2013)).

<sup>189</sup> See Transcript of Oral Argument, *supra* note 138, at 26–28, 36, 48, 57.

<sup>190</sup> See *id.* at 54–55.

<sup>191</sup> See *Quill*, 504 U.S. at 308.

<sup>192</sup> See, e.g., *J. McIntyre Machinery Ltd. v. Nicaastro*, 131 S. Ct. 2780, 2792 (2011) (Breyer, J., concurring). Justice Breyer, who authored the concurring opinion in *McIntyre* that focused on this point, see *id.*, also explored the issue at the *Wayfair* oral argument. See Transcript of Oral Argument, *supra* note 138, at 24.

<sup>193</sup> See *Quill*, 504 U.S. at 319–20 (Scalia, J., concurring); *Wayfair*, 138 S. Ct. at 2093.

<sup>194</sup> See Fatale, *supra* note 22, at 622–25. In general, this is because adjudicative jurisdiction raises difficult questions about choice of law and full faith and credit—questions that do not generally arise in the state tax context. See *id.* Also, in the state tax context, invariably—unlike in many of the adjudicative jurisdiction cases—the commercial actor will have targeted the economic market of the taxing state. See *id.* at 619–22.

*Wayfair* also commented on the specific in-state contacts of the respondents, large Internet vendors. The Court noted that, given the facts, “nexus is clearly sufficient based on both the economic and virtual contacts respondents have with the State.”<sup>195</sup> The respondents’ economic contacts exceeded the state’s statutory nexus thresholds—thresholds which the Court stated each respondent “easily meets.”<sup>196</sup> The Court also noted that the respondents were “large, national companies that undoubtedly maintain an extensive virtual presence.”<sup>197</sup> Although there were no specific facts in evidence on this point, the Court suggested that a modern vendor engaged in e-commerce likely would have a website that leaves “cookies saved to [its] customers’ hard drives” or an app that its customers could download onto their phones.<sup>198</sup> The Court also said that such a vendor might make use of an in-state “virtual showroom.”<sup>199</sup>

One other aspect of due process suggested by *Wayfair* pertains to the prospect that a state might seek to apply a use tax collection nexus law like that of South Dakota retroactively. As due process jurisdiction requires notice or fair warning,<sup>200</sup> retroactive taxation can potentially raise due process concerns. This is particularly so in the context of a use tax collection duty, since to perform this collection the vendor needs to have knowledge of the rule at the time of the transaction. *Wayfair* generally discusses the retroactivity issue as suggesting one way a state might engage in discrimination or impose an undue burden on a taxpayer—claims that would arise under the Commerce Clause and not the Due Process Clause.<sup>201</sup>

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<sup>195</sup> *Wayfair*, 138 S. Ct. at 2099. Cf. *Quill*, 504 U.S. at 307, 312 (noting that the due process test is “minimum contacts”).

<sup>196</sup> *Wayfair*, 138 S. Ct. at 2089.

<sup>197</sup> *Id.* at 2099. It also made reference to “the continuous and pervasive virtual presence of retailers” and their “substantial virtual connections.” *Id.* at 2095.

<sup>198</sup> *Id.* The Court made reference to the fact that two states, Massachusetts and Ohio, had rules that specifically asserted jurisdiction on this basis. *Id.* at 2098–99 (citing 830 MASS. CODE REGS. 64 H.1.7 (2017) and OHIO REV. CODE ANN. § 5741.01(I)(2)(c)(1) (2018)). Similarly, *Quill* had suggested that if a remote vendor owned or otherwise had a property interest in a significant amount of in-state software that ownership interest would confer an in-state physical presence. See *Quill*, 504 U.S. at 315 n.8.

<sup>199</sup> *Wayfair*, 138 S. Ct. at 2094–95. Some persons have noted that the “substantial virtual connections” of an out-of-state vendor like those at issue in the case, *id.* at 2095, could have the effect of causing the vendor to lose the state corporate income tax protection that might otherwise be conferred by the federal statute, commonly referred to as Public Law 86-272. See Act of Sep. 14, 1959, Pub.L. No. 86-272, § 101, 73 Stat. 555). See, e.g., Jaye Calhoun & William J. Kolarik II, *Implications of the Supreme Court’s Historic Decision in Wayfair*, TAX NOTES (July 23, 2018), <https://www.taxnotes.com/state-tax-today/sales-and-use-taxation/implications-supreme-courts-historic-decision-wayfair/2018/07/23/28661> [<http://perma.cc/W4KV-JJ2L>].

<sup>200</sup> See *Quill*, 504 U.S. at 308, 312.

<sup>201</sup> See *Wayfair*, 138 S. Ct. at 2099 (“South Dakota’s tax system includes several features that appear designed to prevent discrimination against or undue burdens upon interstate commerce. . . . [including that] the Act ensures that no obligation to remit the sales tax may be applied retroactively.”); see also *supra* note 145 and accompanying text.

But that may be because *Wayfair* involved primarily a Commerce Clause and not a due process claim. *Wayfair* generally acknowledged that other non-Commerce Clause arguments might also be available to prospective claimants and suggested that due process would be a basis for one such argument.<sup>202</sup>

## D. Undue Burden

### 1. Background and Derivation

The most confusing aspect of *Wayfair* is the undue burden analysis. Both *Bellas Hess* and *Quill* made reference to the burdens that could be faced by vendors seeking to comply with the states' use tax collection duties, though neither holding was justified primarily on that basis. *Bellas Hess* was primarily premised on the notion that mail-order sales are intrinsically interstate transactions, and therefore could not be subject to state tax under the Court's pre-existing Commerce Clause doctrine.<sup>203</sup> That notion was later rejected by the Supreme Court in *Complete Auto*.<sup>204</sup> *Quill* was primarily justified on the theory that mail-order vendors had relied upon *Bellas Hess* for twenty-five years and that the Court should therefore respect this reliance interest.<sup>205</sup> *Quill* recognized that the legal underpinnings for *Bellas Hess* had been removed, and so sought to buttress its decision on some other Commerce Clause basis.<sup>206</sup> Also, the Court considered the matter one that could best be resolved by Congress.<sup>207</sup> Identifying an independent Commerce Clause rationale allowed the Court to bifurcate *Quill's* Commerce Clause and Due Process Clause analyses, and thereby specifically suggest re-consideration by Congress.<sup>208</sup>

*Quill* implicitly distinguished between the imposition of a use tax collection duty and the levy of a state tax. *Quill* analogized the former duty to a state's regulation of a commercial actor, as opposed to the levy of a state tax, and, in so doing, referenced the dormant Commerce Clause balancing

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<sup>202</sup> *Wayfair*, 138 S. Ct. at 2099 (“[I]f some small businesses with only *de minimis* contacts seek relief from collection systems thought to be a burden, those entities may still do so under other theories.”) (emphasis added). See *Quill*, 504 U.S. at 305 (“If there is a want of due process to sustain the tax, by that fact alone any burden the tax imposes on the commerce among the states becomes ‘undue.’”) (quoting *International Harvester Co. v. Department of Treasury*, 322 U.S. 340, 353 (1944) (Rutledge, J., concurring in part and dissenting in part)).

<sup>203</sup> *Nat'l Bellas Hess v. Dep't of Revenue*, 386 U.S. 753, 759–760 (1967).

<sup>204</sup> See *Wayfair*, 138 S. Ct. at 2091; see also *supra* notes 40–42 and accompanying text.

<sup>205</sup> See *supra* notes 62–63 and accompanying text.

<sup>206</sup> See *supra* note 85 and accompanying text.

<sup>207</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298, 318 (1992).

<sup>208</sup> *Id.*; see also *supra* note 85 and accompanying text.



test from *Pike v. Bruce Church, Inc.*<sup>209</sup> Under *Pike*'s "undue burden" test, "[s]tate laws that 'regulat[ed] even-handedly to effectuate a legitimate local public interest . . . will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits.'"<sup>210</sup> But *Quill* did not engage in any balancing or set forth a test that would require balancing—it merely utilized the notion of an undue burden as the basis for the creation of the Court's "bright-line physical presence" rule.<sup>211</sup> The Court's theory was that application of the physical presence rule would police against undue burdens resulting from the imposition of a use tax collection duty.<sup>212</sup> Also, the Court's physical presence rule would protect the mail-order reliance interests created by *Bellas Hess*, because the physical presence rule subsumed the holding of that earlier case. But the *Quill* Court's overriding rationale seemed to be that, however faulty its case logic, Congress would soon act to address the mail-order use tax issue—which of course it never did.<sup>213</sup> Three of the eight Justices in *Quill*—including Justices Kennedy and Thomas, both of whom were in the *Wayfair* majority—disagreed with *Quill*'s Commerce Clause reasoning and said that they would support the holding only on the basis of stare decisis.<sup>214</sup>

In *Wayfair*, the undue burden test was first considered in the context of the Court's rejection of the argument that stare decisis would require retention of the physical presence rule.<sup>215</sup> *Wayfair* revisited the question in *Quill* whether retention of the rule could be justified solely on the basis of stare decisis.<sup>216</sup> The Court concluded that it could not be, because physical presence is not a "clear or easily applicable standard."<sup>217</sup> Also, the Court noted that "*stare decisis* accommodates only 'legitimate reliance interest[s]'" and, contrary to such reliance, some Internet vendors had been aggressively using the physical presence rule to avoid tax and to obtain a market advantage.<sup>218</sup> The Court stated that

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<sup>209</sup> See *supra* notes 67–69 and accompanying text.

<sup>210</sup> See *South Dakota v. Wayfair Inc.*, 138 S. Ct. 2080, 2091 (2018) (quoting *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970)) (emphasis added).

<sup>211</sup> *Quill*, 504 U.S. at 314–15, 317.

<sup>212</sup> *Id.* See *Wayfair*, 138 S. Ct. at 2092 (noting "the *Quill* majority concluded that the physical presence rule was necessary to prevent undue burdens on interstate commerce").

<sup>213</sup> See *supra* note 85 and accompanying text.

<sup>214</sup> See *Wayfair*, 138 S. Ct. at 2092 (citing *Quill*, 504 U.S. at 320) (noting the concurring opinion in *Quill* of Justice Scalia, which was joined by Justices Kennedy and Thomas).

<sup>215</sup> *Id.* at 2096–98.

<sup>216</sup> *Id.*

<sup>217</sup> *Id.* at 2098. The dissent split with the majority on this issue. See *id.* at 2101–02 (Roberts, C.J., dissenting).

<sup>218</sup> *Id.* at 2096, 2098 (emphasis in original) (internal citation omitted).



“constitutional right[s]” do not logically follow from “practical opportunities [to engage in] tax avoidance.”<sup>219</sup>

*Wayfair* nonetheless remained sympathetic to the burdens that the states’ use tax collection duties could impose upon smaller remote vendors selling over the Internet. The Court said that “the daunting complexity and business-development obstacles of nationwide sales tax collection” will result in burdens that “may pose legitimate concerns in some instances, particularly for small businesses that make a small volume of sales to customers in many States.”<sup>220</sup> *Wayfair* referred sympathetically to such smaller vendors nine times.<sup>221</sup> It was in response to these concerns that the Court noted the potential prospect of such vendors bringing a claim using the *Pike* undue burden standard.<sup>222</sup>

The *Wayfair* Court’s references to the undue burden test seem intended to encourage the states to be fair in their implementation of that decision and to otherwise simplify their use tax collection laws, if appropriate. When evaluating this general issue *Wayfair* referenced the fact that South Dakota law already “affords small merchants a reasonable degree of protection.”<sup>223</sup> Specifically, the Court referred to: (1) South Dakota’s high statutory nexus thresholds, as discussed above; (2) the fact that the South Dakota statute was not retroactive; and (3) the fact that South Dakota was “one of more than [twenty] States that have adopted the Streamlined Sales and Use Tax Agreement. . . . [which] standardizes taxes to reduce administrative and compliance costs . . .”<sup>224</sup> Hence, the Court encouraged—though did not require—other states to adopt similar measures. As noted earlier, however, the first two legal protections—reasonably high nexus thresholds and prospective

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<sup>219</sup> *Id.* at 2098 (internal citation omitted). The Court cited one case for its statement concerning legitimate reliance interests and through that citation, intentionally or not, analogized the large Internet vendors who had exploited the physical presence rule to wrongdoers. *See id.* (citing *United States v. Ross*, 456 U.S. 798, 824, which concluded that narcotics smugglers had no “legitimate reliance interest” with respect to the Court’s prior Fourth Amendment search and seizure precedent because these persons had used that precedent to structure their unlawful businesses). *See also Ross*, 456 U.S. at 824 & n.3.

<sup>220</sup> *Wayfair*, 138 S. Ct. at 2098.

<sup>221</sup> *See id.* at 2093, 2098–99.

<sup>222</sup> *Id.* at 2098–99. Given the Court’s longstanding, general notion that it should refrain from restricting state sovereignty under the dormant Commerce Clause other than in instances of state discrimination, *see supra* notes 95 and 146 and accompanying text, it seems fair to question the Court’s emphasis on protecting small out-of-state vendors. The Commerce Clause was not intended to protect any particular class of vendors, *see generally* U.S. CONST. art I, § 8, cl. 3., and the Court’s emphasis on singling out small vendors for protection seems to be nothing more than a policy determination that is legislative in its nature.

<sup>223</sup> *Wayfair*, 138 S. Ct. at 2098.

<sup>224</sup> *Id.* at 2099–100.

enforcement—may be otherwise generally necessary as a matter of due process.<sup>225</sup>

## 2. Problems with the Standard

The Court's attempt to prod the states to simplify their sales tax systems for smaller vendors seems laudable. Perhaps it was even necessary to get the Court to a majority of five votes, as concern about the potential tax collection burden to be imposed upon smaller vendors was certainly an important issue for the Justices at oral argument.<sup>226</sup> But the Court's references to the undue burden standard were half-hearted, vague, not clearly supported by all five Justices in the majority, and make little conceptual or practical sense.

The *Wayfair* majority invoked the undue burden standard in a peculiar way. The Court stated that “the United States argues that *tax-collection requirements* should be analyzed under the balancing framework of *Pike v. Bruce Church, Inc.*”<sup>227</sup> The United States did in fact argue in favor of applying the undue burden test to the states' use tax collection laws in both its *Wayfair* amicus brief and at oral argument.<sup>228</sup> But the Court's lukewarm endorsement of this point—attributing it not to its own legal conclusions but to the thoughts of one of the amici—suggests ambivalence. This is not surprising since the Court has been retreating from the *Pike* undue burden test for several decades, even in the regulatory context from which that standard derives.<sup>229</sup>

More specifically, *Wayfair*'s reference to the *Pike* undue burden standard is inconsistent with the overruling of *Quill*. That overruling was intended to eliminate preferential treatment of remote vendors and to dispense with artificial taxpayer

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<sup>225</sup> See *supra* notes 186–188 and 200–202 and accompanying text; see also John A. Swain, *State Sales and Use Tax Jurisdiction: An Economic Nexus Standard for the Twenty-First Century*, 38 GA. L. REV. 343, 345 (2003) (“[A]nyone making taxable sales within the taxing jurisdiction should have a collection obligation, subject to a de minimis threshold below which the cost of collection exceeds the benefit.”); see also Adam B. Thimmesch, *The Illusory Promise of Economic Nexus*, 13 FLA. TAX REV. 157, 199 (2012) (“[A] state need only set its threshold amounts high enough to effectively eliminate any unreasonable risk that taxpayers will exceed them without having expended constitutionally significant efforts to exploit the market.”).

<sup>226</sup> See generally Transcript of Oral Argument, *supra* note 138.

<sup>227</sup> *Wayfair*, 138 S. Ct. at 2099 (emphasis added).

<sup>228</sup> See Transcript of Oral Argument, *supra* note 138 at 26–27; Brief for the United States as Amicus Curiae Supporting Petitioner at 13, 17–23, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2084 (2018) (No. 17-494).

<sup>229</sup> See *Fatale*, *supra* note 81, at 60–62 (describing the Court's general concerns with *Pike* balancing dating back to the time of *Quill*); see also Rothfeld, *supra* note 85, at 489 (“[G]iven the (largely justified) criticism of the *Pike* approach as a standardless and subjective means of applying the Commerce Clause, it is more than a little surprising that the Court chose to expand *Pike* balancing in the tax area.” (footnote omitted)).

distinctions.<sup>230</sup> Instead, by suggesting that an undue burden can be claimed by small remote vendors but not small out-of-state vendors that have an in-state physical presence, the Court served to perpetuate—at least in part—similar distinctions.<sup>231</sup> Clearly, physically present vendors can be in all other respects identical to remote vendors, and therefore face identical compliance burdens—and yet they are not the vendors *Wayfair* sought to protect. Therefore, unlike their remote vendor competitors, small multistate vendors that have in-state physical presence would apparently not be able to maintain an undue burden claim. This follows because *Wayfair* did not alter pre-existing jurisdictional principles; it merely sought to eliminate the physical presence rule, and to explain the effect of that elimination on vendors that were formerly protected.<sup>232</sup>

The undue burden standard was introduced into the state tax area by *Quill*—specifically to prop up the Court’s newly-posed physical presence rule.<sup>233</sup> The application of the undue burden standard in the state tax area was unclear, but on the other hand, as posited in *Quill*, did not need to be put to the test, because the standard was merely one predicate that the Court used to adopt its “bright-line” physical presence rule.<sup>234</sup> It was physical presence—and the three other prongs of the pre-existing *Complete Auto* test—that were to address “undue burdens.”<sup>235</sup> This meant that the mechanics of specifically evaluating undue burden in the state tax area was, if anything, just a conceptual idea lurking in the background.

Justice Kennedy, who wrote the *Wayfair* decision, did not join the section in *Quill* that referenced undue burden making his seeming, even if lukewarm, endorsement of that standard in *Wayfair* more mystifying. When *Wayfair* cites criticism of the physical presence rule—something it says has “been the target of criticism over many years from many quarters”—it cites only a

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<sup>230</sup> See *Wayfair*, 138 S. Ct. at 2092–94.

<sup>231</sup> Cf. *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 364 (1941) (noting that once the state has extended to a mail-order vendor the privilege to do business in the state, the state may exact “this burden [of tax collection] as a price of enjoying the full benefits flowing from its [in-state] business”). See also Rothfeld, *supra* note 85, at 490 (questioning *Quill*’s concern with the burdens imposed upon remote vendors when the burden for comparable vendors with physical presence is identical).

<sup>232</sup> See *supra* notes 158–166 and 177 and accompanying text.

<sup>233</sup> See Rothfeld, *supra* note 85, at 488 (noting that prior to *Quill* the Court had not applied *Pike* balancing in a tax case); see also *supra* notes 82–85 and accompanying text.

<sup>234</sup> See *supra* notes 86–87 and accompanying text.

<sup>235</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298, 312–15 (1992); see also *Fatale*, *supra* note 22, at 592–93.

single article.<sup>236</sup> And that article, immediately after the page cited, criticizes the invocation of undue burden analysis in the context of the use tax collection duty, stating that it “cannot be reconciled with prior decisions of the Court.”<sup>237</sup> That same article also states that the undue burden analysis, as so invoked, “suffer[s] from serious logical flaws.”<sup>238</sup>

In general, state tax cases since the time of *Quill* do not rely on or even evaluate the application of the undue burden test. This is because, as noted, *Quill* made clear that in the state tax context the undue burden analysis is not a stand-alone test, but rather merely a concern that is addressed by the four prongs of *Complete Auto*, including the nexus requirement.<sup>239</sup> The Court has stated, in *Japan Line, Ltd. v. County of Los Angeles*<sup>240</sup> that, when those four prongs are met, “no impermissible burden on interstate commerce will be found . . . .”<sup>241</sup> When *Wayfair* stated its rule pertaining to state tax nexus, it cited to language in *Polar Tankers, Inc. v. City of Valdez*,<sup>242</sup> and those cited pages in turn referenced the analysis in *Japan Line* that included this statement.<sup>243</sup> Also, since the time of *Quill* no case has found that a state tax imposed an undue burden on interstate commerce, apart from consideration of the *Complete Auto* standards.<sup>244</sup>

Further, the two concurring Justices in *Wayfair*, Justices Thomas and Gorsuch, both limited their approval of the majority’s decision to the holding—the eradication of the physical presence rule.<sup>245</sup> Both Justices criticized the Court’s dormant Commerce Clause jurisprudence more generally<sup>246</sup>—and *Pike* balancing is one prominent component of that jurisprudence.<sup>247</sup> Justice Thomas previously joined Justice Scalia’s dissent in a state case decided three years before *Wayfair* that critiqued the dormant Commerce Clause as “a judge-invented rule under which judges may set aside state laws that they think impose too much of a burden upon

<sup>236</sup> *Wayfair*, 138 S.Ct. at 2092 (quoting *Direct Mktg. Ass’n v. Brohl*, 814 F.3d 1129, 1148 (10th Cir. 2016) (Gorsuch, J., concurring) (citing Rothfeld, *supra* note 85)).

<sup>237</sup> Rothfeld, *supra* note 85, at 489.

<sup>238</sup> *Id.*

<sup>239</sup> See *supra* note 235 and accompanying text.

<sup>240</sup> 441 U.S. 434 (1979).

<sup>241</sup> *Id.* at 444–45.

<sup>242</sup> *Wayfair*, 138 S. Ct. at 2099 (citing *Polar Tankers, Inc. v. City of Valdez*, 557 U.S. 1, 11 (2009)).

<sup>243</sup> *Polar Tankers, Inc.*, 557 U.S. at 11 (citing *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 441–45 (1979)).

<sup>244</sup> *Fatale*, *supra* note 22, at 593–94, 594 n.157.

<sup>245</sup> *Wayfair*, 138 S. Ct. at 2100 (Thomas, J., concurring); *id.* at 2100–01 (Gorsuch, J., concurring).

<sup>246</sup> *Id.* at 2100 (Thomas, J., concurring); *id.* at 2100–01 (Gorsuch, J., concurring).

<sup>247</sup> See *Fatale*, *supra* note 81, at 60–62.

interstate commerce.”<sup>248</sup> Justice Gorsuch in his *Wayfair* concurrence favorably cited that same Scalia dissent.<sup>249</sup>

### 3. Practical Application

Given the above analysis, it seems unlikely that the Court itself would actually apply the undue burden standard to a use tax collection duty. So, why then mention it? As noted, the Court seemed to be encouraging the states to be fair in their administration of *Wayfair*. Suggesting that there is some legal standard that could sit in judgment of the states’ actions—however unlikely or unclear that standard may be—arguably tends to serve that purpose, if only because state personnel, like most persons, tend to fear the unknown. Also, the Court is not likely to be the adjudicator of later undue burden claims, should they manifest. That test would relate to the determination of state tax nexus, and before *Wayfair* the Court had not taken a nexus case in twenty-five years—despite repeated certiorari petitions in state tax cases.<sup>250</sup> The Court’s calculus seemed to be to relegate questions concerning undue burden to the state courts, and then assume that those courts will police these burdens—presumably understanding the problem, and knowing the solution, in the context of specific cases.<sup>251</sup>

What an undue burden litigation claim might look like and who would bring one (including in what state) is an open question. *Pike* itself suggests the dilemma, as in that case the Court struck down an order issued pursuant to a statute enacted by the state of Arizona that would require persons that grew cantaloupes in the state to pack the cantaloupes in-state and to identify that the cantaloupes were from an Arizona packer.<sup>252</sup> The difficulty for the grower was that it did not pack its cantaloupes in Arizona, but rather shipped them to its packing facility in California, where they were not labeled as packed in

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<sup>248</sup> See *Comptroller of the Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1807–08 (2015) (Scalia, J., dissenting).

<sup>249</sup> See *Wayfair*, 138 S. Ct. at 2101 (Gorsuch, J., concurring) (citing *Wynne*, 135 S. Ct. at 1807 (2015) (Scalia, J., dissenting)).

<sup>250</sup> See *Fatale*, *supra* note 22, at 583–84 n.106.

<sup>251</sup> See Darien Shanske, *Wayfair as Federalism Decision*, MEDIUM (June 4, 2018), <https://medium.com/whatever-source-derived/wayfair-as-federalism-decision-16577e592a6b> [<http://perma.cc/2TNF-8T24>] (“The Court in *Wayfair* does not explicitly shift to a kind of balancing test (in particular, *Pike* balancing), but its retention of a ‘substantial nexus’ standard without much further guidance seems to invite the states to engage in balancing.”); Maria Koklanaris, *4 Constitutional Questions To Ponder In A Post-Quill World*, LAW360 (June 29, 2018, 8:11 PM), <https://www.law360.com/articles/1058921/4-constitutional-questions-to-ponder-in-a-post-quill-world> (citing tax practitioner opinions for the view that *Wayfair* embodies “a nudge to states not to impose undue burdens lest they be checked”).

<sup>252</sup> *Pike v. Bruce Church*, 397 U.S. 137, 138–40, 146 (1970).

Arizona.<sup>253</sup> The Court concluded that the Arizona statute was too burdensome as applied to the grower, where the grower would have had to expend an extra \$200,000 to pack a \$700,000 crop.<sup>254</sup>

In the context of the use tax collection duty, *Pike* would seem to suggest that one is to compare the taxpayer's costs of compliance with the revenue benefits to the state from the collected tax.<sup>255</sup> But that is an apples and oranges comparison that would seem to turn on entirely subjective considerations as to what value one attributes to the tax.<sup>256</sup> The subjectivity that is inherent in the *Pike* balancing test as applied in the regulatory context is the very essence of why the Court has retreated from the test in recent years.<sup>257</sup> Also, if one is to apply the test to the use tax collection duty, it is hard to see how, in light of *Wayfair*, a state that adopts South Dakota-like thresholds could fail. In *Pike*, the Court recognized the state's interest in its cantaloupe statute as being "legitimate," but not "compelling."<sup>258</sup> In contrast, *Wayfair* emphasized the critical importance of the states' tax collection function.<sup>259</sup>

*Pike* also suggests that a state law could fail its test if there is a less onerous state way to achieve the same result.<sup>260</sup> But the

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<sup>253</sup> *Id.* at 139.

<sup>254</sup> *Id.* at 140, 145–46.

<sup>255</sup> Justice Breyer—who did not join the *Wayfair* majority opinion—suggested as much at the oral argument, commenting that the inquiry would seemingly be to determine whether “the benefits of state revenue do not outweigh the compliance costs associated with the tax collection obligations that the state has imposed.” See Transcript of Oral Argument, *supra* note 138, at 57. Justice Breyer recognized such an inquiry could unleash significant litigation. See *id.*

<sup>256</sup> *Cf.* *Dep't of Revenue of Ky. v. Davis*, 553 U.S. 328, 355 (2008) (“What is most significant about these [*Pike*] cost-benefit questions is not even the difficulty of answering them or the inevitable uncertainty of the predictions that might be made in trying to come up with answers, but the unsuitability of the judicial process and judicial forums for making whatever predictions and reaching whatever answers are possible at all.”); *id.* at 355–56 (“Courts as institutions are poorly equipped to evaluate with precision the relative burdens of various methods of taxation. The complexities of factual economic proof always present a certain potential for error, and courts have little familiarity with the process of evaluating the relative economic burden of taxes.”) (quoting *Fulton Corp. v. Faulkner*, 516 U.S. 325, 342 (1996)).

<sup>257</sup> See *Fatale*, *supra* note 81, at 60–62. It is for similar reasons that the Court backed away from its early twentieth century dormant Commerce Clause doctrine that considered whether a taxpayer's in-state activity was interstate or intrastate. See *supra* notes 23–25 and accompanying text.

<sup>258</sup> See *Pike*, 397 U.S. at 143–46 (stating that the “regulatory scheme could perhaps be tolerated if a more compelling state interest were involved” but that “the State's interest is minimal at best—certainly less substantial than a State's interest in securing employment for its people”).

<sup>259</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2088, 2095 (2018); see also *Fatale*, *supra* note 81, at 42 n.3 (citing cases).

<sup>260</sup> See *Pike*, 397 U.S. at 142 (“If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.”).



difficulty with this logic, as transposed to the state tax context, is that it will probably always be the case that a tax system could be made simpler with modest reductions in revenue. Yet, this alone would seem to be insufficient grounds for striking down an entire “tax system.”<sup>261</sup> That result certainly seems inconsistent with *Wayfair*'s pro-state sovereignty analysis.<sup>262</sup>

*Wayfair* implied that the only vendors that could logically bring an undue burden claim would be small remote vendors, as they would have the greatest difficulty with the tax implications resulting from the case.<sup>263</sup> It is not inconceivable, for example, that—at least hypothetically—a smaller vendor would have to incur what for it could be significant costs to pay a tax to a specific state that would be, in dollar terms, less significant. But if the state's nexus thresholds were to at least mirror that of South Dakota, it is hard to see how—at least applying *Wayfair*'s analysis—so small a vendor could ever become subject to the state's law.<sup>264</sup> Larger vendors—the vendors that *Wayfair* accused of using *Quill* to unfairly avoid tax collection<sup>265</sup>—would more likely be the persons seeking to enjoin a state's law. But *Wayfair* suggested that because larger vendors have greater means to comply, they would be less likely to have an undue burden claim.<sup>266</sup>

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<sup>261</sup> See *Wayfair*, 138 S. Ct. at 2099.

<sup>262</sup> See *supra* notes 133–137 and accompanying text. *Wayfair* referenced only one other burdens-type case, *S. Pac. Co. v. Arizona*, 325 U.S. 761 (1945), which preceded *Pike*. See *Wayfair*, 138 S. Ct. at 2091. *Southern Pacific* makes even less sense as applied in the state tax context. See *supra* notes 71–81 and accompanying text.

<sup>263</sup> The majority made nine references to small businesses. See *Wayfair*, 138 S. Ct. at 2093, 2098–99. The dissent expressed sympathy for small businesses as well. See *id.* at 2104. (Roberts, C.J., dissenting). In contrast, the majority viewed larger vendors as bad actors that had attempted to manipulate the *Quill* physical presence rule. See *id.* at 2098 (“Some remote retailers go so far as to advertise sales as tax free. A business ‘is in no position to found a constitutional right on the practical opportunities for tax avoidance.’” (internal citations omitted) (quoting *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 366 (1941))). See also *supra* notes 218–219 and accompanying text. The Court's citation for this proposition was to the brief of the petitioner, South Dakota, which quoted the respondent *Wayfair*'s website. See *id.* (citing Petitioner's Brief, *supra* note 138, at 55). See also *id.* at 2099 (“[R]espondents are large, national companies that undoubtedly maintain an extensive virtual presence.”); see also *id.* (acknowledging that there could be legal questions about state implementation of its decision but concluding that prospect “cannot justify retaining [an] anachronistic rule that deprives States of vast revenues from major businesses”).

<sup>264</sup> See *id.* at 2098 (noting that “the law at issue requires a merchant to collect the tax only if it does a considerable amount of business in the State” and that the law “applies a safe harbor to those who transact only limited business in [the state]”).

<sup>265</sup> See *id.* at 2093, 2098–99, 2104. See also *supra* note 263 and accompanying text.

<sup>266</sup> See *id.* at 2098–99. See Walter Hellerstein and Andrew Appleby, *Substantive and Enforcement Jurisdiction in a Post-Wayfair World*, *Tax Analysts*, STATE TAX TODAY (Oct. 22, 2018) (“It may be difficult for large, sophisticated remote sellers to avoid a sales and use tax collection obligation under the *Pike* balancing test. The Court has recognized that imposing such obligations on sellers is a ‘familiar and sanctioned device,’ and that the ‘sole burden imposed upon the out-of-state seller . . . is the administrative one of collecting



The nature of sales tax is such that a larger vendor with the means to comply with a state's law would almost certainly have to comply with that law or could be ultimately responsible for paying the tax that it failed to collect from consumers out of its own pocket. On the other hand, a vendor in full compliance with a state's use tax collection law would seemingly face a difficult hurdle in attempting to claim that this collection activity was nonetheless unduly burdensome. That same general issue would apparently lurk also if the vendor was collecting use tax in most states but not the state in question. In that case, the vendor would have to justify its disparate approach in the latter state.

In any lawsuit claiming that a state tax is unconstitutional, there is a question as to whether the claim is that the statute is "facially" unconstitutional, i.e., is not valid on any conceivable set of facts, or unconstitutional "as applied" to the taxpayer.<sup>267</sup> *Wayfair* vaguely suggested that an undue burden challenge could result in the invalidity of a state statute<sup>268</sup>—a potential result that could apparently occur only in the context of a facial challenge. But conversely the essence of an undue burden challenge would necessarily seem to be a "case-by-case evaluation."<sup>269</sup> Certainly, the repeated statements in *Wayfair* to the effect that only smaller vendors could logically maintain an undue burden claim indicates that a successful facial challenge would be unlikely; a small vendor could have a reasonable as applied claim, but the state law would presumably remain valid as to larger vendors.

One other issue that arises when considering a potential undue burden claim pertains to the desired outcome. In the past, vendor litigation concerning the physical presence standard was intended to broaden the states' interpretation of that standard because, once broadened, all taxpayers—including the litigant—would benefit from that expanded interpretation on a going forward basis. But a determination that a state tax system is too burdensome in a particular respect—e.g., because the nexus thresholds are too low—would presumably provide a road map to the state as to how

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[the tax].") (quoting *Gen. Trading Co. v. State Tax Comm'n*, 322 U.S. 335, 338 (1944) and *Nat'l Geographic Soc'y v. Cal. Bd. of Equalization*, 430 U.S. 551, 558 (1977)).

<sup>267</sup> See *Overstock.com, Inc. v. N.Y. State Dept. of Taxation & Fin.*, 987 N.E.2d 621, 624 (N.Y. 2013).

<sup>268</sup> *Wayfair*, 138 S. Ct. at 2099 ("The question remains whether some other principle in the Court's Commerce Clause doctrine might invalidate the Act.").

<sup>269</sup> See *Quill Corp. v. North Dakota*, 504 U.S. 313, 314–15 (1992). *Pike* itself resulted in only a specific case determination as to the litigant. See *Pike v. Bruce Church*, 397 U.S. 137, 140, 145–46 (1970); see also *Wayfair*, 138 S. Ct. at 2094 ("The Court's Commerce Clause jurisprudence has 'eschewed formalism for a sensitive, case-by-case analysis of purposes and effects.'" (citing *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 201 (1994))).

to fix the problem. The upshot is that most non-claimant taxpayers subject to the law would likely be unaffected by such a ruling because it would likely be an as applied determination. And, because the state would probably act to amend its law in response to the decision, even a victorious taxpayer could end up collecting the tax in short order anyway.

The above analysis suggests that there may not be much undue burden litigation in the aftermath of *Wayfair*. But that could be wishful thinking. For example, *Quill* clearly suggested that the physical presence rule was limited to the states' use tax collection duty, but that did not prevent twenty-five years' worth of litigation addressing whether the standard had broader application.<sup>270</sup> It would of course be ironic if *Wayfair* unleashed a quarter-century of cases on a question that seems specious because *Quill* did the same thing, and one of *Wayfair's* purposes was to reject the calamitous after-effects of *Quill*.

## V. CONCLUSION

*Wayfair* eradicated the nonsensical physical presence nexus requirement that the Court had created in *Bellas Hess* and *Quill*. The Court thereby effectively completed, more than one-half century later, a trend in its dormant Commerce Clause cases that commenced in the mid-part of the Twentieth Century—reversing the conclusion that free trade considerations impose limitations on the state tax jurisdiction rules that apply to multi-state companies engaged in business in a state.

Though it dispensed with the idea that certain large companies doing business across state lines are sometimes entitled to state tax immunity, *Wayfair* expressed concern with the compliance costs of the use tax collection duty as applied to smaller multi-state businesses. To address these concerns, the Court repeated the error of *Bellas Hess* and *Quill* and posited a vague new legal test, pertaining to “undue burden,” that has no basis in the Court’s prior state tax cases. Ironically, the notion of transposing the undue burden concept to the state tax context traces entirely to the analysis in *Quill* that *Wayfair* otherwise rejected. Further, because the undue burden test has never been actually applied to state tax cases, it is not apparent how it could apply. Hence the concept has the prospect of unleashing the same type of confusion and litigation that followed in the aftermath of *Quill*.

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<sup>270</sup> See Fatale, *supra* note 22, at 583–84 n.106; see also generally *Capital One Auto Fin., Inc. v. Dep't of Revenue*, 22 Or. Tax 326 (2016), *affirmed*, 363 Or. 441 (2018).

*Wayfair* noted correctly that “[t]he physical presence rule is a poor proxy for the compliance costs faced by companies that do business in multiple States.”<sup>271</sup> It also stated that “[o]ther aspects of the Court’s doctrine can better and more accurately address any potential burdens on interstate commerce, whether or not *Quill*’s physical presence rule is satisfied.”<sup>272</sup> But the Court did not need to posit a new, poorly-considered state tax test to help to accomplish these goals. The elimination of the physical presence rule means that the primary nexus standard to be applied when evaluating state tax jurisdiction is due process, which adequately addresses the state tax burdens to be faced by smaller—as well as all other—multistate businesses. Due process requires that a state tax be adequately noticed, otherwise fair, and applied to remote vendors engaged in significant in-state market exploitation. When these standards are met, there is no issue as to undue burden. The Court’s robust anti-discrimination principle addresses all other constitutional concerns.<sup>273</sup>

*Wayfair* stated that “[i]f it becomes apparent that the Court’s Commerce Clause decisions prohibit the States from exercising their lawful sovereign powers in our federal system, the Court should be vigilant in correcting the error.”<sup>274</sup> It seems patent that the Court did not issue *Wayfair* with the intent to actively evaluate future state tax nexus claims.<sup>275</sup> Also, due process considerations are sufficient to evaluate such claims. Nonetheless, the Court should remain vigilant to one day revisit *Wayfair* and thereby correct its erroneous undue burden test.

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<sup>271</sup> *Wayfair*, 138 S. Ct. at 2093.

<sup>272</sup> *Id.*

<sup>273</sup> *See supra* notes 95 and 146 and accompanying text.

<sup>274</sup> *Wayfair*, 138 S. Ct. at 2096.

<sup>275</sup> *See supra* notes 250–251 and accompanying text.

# Comparing *Wayfair* and *Wynne*: Lessons for the Future of the Dormant Commerce Clause

*Edward A. Zelinsky\**

## I. INTRODUCTION

This Article compares the Supreme Court's dormant Commerce Clause decisions in *South Dakota v. Wayfair*<sup>1</sup> and *Comptroller of the Treasury of Maryland v. Wynne*.<sup>2</sup> *Wayfair* and *Wynne* are both as important, as they were narrowly-decided. Despite (perhaps because of) their differences, they together tell us much about the current Court's divisions under the dormant Commerce Clause and about the future of the dormant Commerce Clause.

A comparison of *Wayfair* and *Wynne* indicates that the prospect of the Court jettisoning the dormant Commerce Clause altogether is unlikely. However, the Justices who would abandon the dormant Commerce Clause can exercise decisive influence in particular cases as they did in *Wayfair*.<sup>3</sup> The current Court's dormant Commerce Clause skeptics—Justices Thomas and Gorsuch—provided the crucial fourth and fifth votes in *Wayfair* to overturn *Quill*.<sup>4</sup>

It will continue to be rare for the Court to reverse its own dormant Commerce Clause decisions. Far from opening the floodgates, *Wayfair* indicates that the Court is reluctant to overrule its dormant Commerce Clause cases in light of Congress's ultimate constitutional power to regulate interstate commerce. However, when neither the Court nor Congress has spoken on a particular issue, the Court will consider extending the dormant Commerce Clause as it did in *Wynne*.<sup>5</sup>

Going forward, an important issue under the dormant Commerce Clause will be the double taxation which results when

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<sup>1</sup> 138 S. Ct. 2080 (2018).

<sup>2</sup> 135 S. Ct. 1787 (2015).

<sup>3</sup> See *Wayfair*, 138 S. Ct. at 2087.

<sup>4</sup> *Id.*

<sup>5</sup> See *Wynne*, 135 S. Ct. at 1794.

an individual is deemed to be a resident for tax purposes, by two states, each of which taxes all of the dual resident's income. *Wayfair* and *Wynne* suggest that, despite the compelling arguments against the double state taxation of dual residents' incomes, the Court will be reluctant to set aside its precedents upholding the double state taxation of dual residents.<sup>6</sup>

Instead, the Court is more likely to extend dormant Commerce Clause protection when states are overly aggressive in taxing the income of nonresidents. In particular, the Court is more likely to apply the dormant Commerce Clause apportionment principle to curb New York's "convenience of the employer" doctrine to avoid New York's double state income taxation of telecommuters on the days they work at their out-of-state homes.<sup>7</sup>

## II. WAYFAIR

By a 5-4 vote, *Wayfair* overturned *Quill Corp. v. North Dakota*<sup>8</sup> as "unsound and incorrect."<sup>9</sup> In 1992, *Quill* confirmed the dormant Commerce Clause rule that a state could impose sales tax collection responsibilities on a retailer only if the retailer had a physical presence in the taxing state.<sup>10</sup> This physical presence rule had first been announced in *National Bellas Hess v. Department of Revenue* in 1967.<sup>11</sup> *Quill* and *Bellas Hess* were decided before the rise of the Internet and electronic commerce. These decisions severely limited the states' abilities to enforce their respective sales taxes on internet purchases by precluding the states from imposing sales tax collection duties on out-of-state internet and mail-order retailers.<sup>12</sup>

In *Wayfair*, Justice Kennedy advanced three basic themes for overturning *Quill* and thereby abolishing the physical presence rule.<sup>13</sup> The first of these *Wayfair* themes was the historic legitimacy of the dormant Commerce Clause which "imposes limitations on the States absent congressional action."<sup>14</sup> A second theme of *Wayfair* was the flaws of *Quill* and of the physical presence rule<sup>15</sup> which

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<sup>6</sup> See *Wayfair*, 138 S. Ct. at 2080; *Wynne*, 135 S. Ct. at 1787.

<sup>7</sup> See generally Edward A. Zelinsky, *New York's "Convenience of the Employer" Rule is Unconstitutional*, 48 ST. TAX NOTES 553 (2008).

<sup>8</sup> 504 U.S. 298 (1992), *overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>9</sup> *Wayfair*, 138 S. Ct. at 2099.

<sup>10</sup> See *id.* at 314.

<sup>11</sup> 86 U.S. 753 (1967), *confirmed by* *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), *and overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>12</sup> For further background on these limitations, see Edward A. Zelinsky, *The Political Process Argument for Overruling Quill*, 82 BROOK. L. REV. 1177, 1180-84 (2017) and Andrew J. Haile, *Affiliate Nexus in E-Commerce*, 33 CARDOZO L. REV. 1803, 1806-12 (2012).

<sup>13</sup> See *Wayfair*, 138 S. Ct. at 2088-97.

<sup>14</sup> *Id.* at 2089.

<sup>15</sup> *Id.* at 2088.

*Quill* perpetuated under the dormant Commerce Clause. That rule, Justice Kennedy wrote, “is not a necessary interpretation” of the substantial nexus test developed under the dormant Commerce Clause.<sup>16</sup> Moreover, that rule “creates rather than resolves market distortions”<sup>17</sup> and embodies an “arbitrary, formalistic distinction”<sup>18</sup> between those types of in-state presence which are deemed to create substantial nexus with the state and those which are not. “In the name of federalism and free markets, *Quill* does harm to both.”<sup>19</sup> Third, Justice Kennedy concluded the Court should disregard the dictates of stare decisis and should itself overturn *Quill* rather than rely on Congress to overrule the “unfair and unjust”<sup>20</sup> physical presence rule.<sup>21</sup>

Concurring with Justice Kennedy’s majority opinion, Justice Thomas reiterated his view that the Court’s dormant Commerce Clause case law “can no longer be rationally justified.”<sup>22</sup> Also concurring, Justice Gorsuch did not go as far as Justice Thomas but, in a skeptical vein, noted that the validity of the Court’s dormant Commerce Clause case law is a “question[ ] for another day.”<sup>23</sup>

Thus, while Justices Thomas and Gorsuch provided the fourth and fifth votes in *Wayfair*, they bottomed their conclusions on different premises than those embraced by Justice Kennedy. For Justice Kennedy (joined by Justices Alito and Ginsburg) the dormant Commerce Clause is a legitimate enterprise which went astray in *Quill*.<sup>24</sup> For Justice Thomas (definitely) and for Justice Gorsuch (probably), *Quill* was not simply a mistake, but rather was the product of the misbegotten project that is the dormant Commerce Clause.<sup>25</sup>

As a matter of substance, Chief Justice Roberts was as critical of the physical presence rule as was Justice Kennedy. On behalf of himself and three of his colleagues, Chief Justice Roberts wrote that *Bellas Hess*, which originally announced the physical presence rule confirmed in *Quill*, “was wrongly decided.”<sup>26</sup> Consequently, not a single member of the *Wayfair* Court concluded that the physical

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<sup>16</sup> *Id.* at 2092.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.* at 2096.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.* at 2096–97.

<sup>22</sup> *Id.* at 2100 (Thomas, J., concurring) (quoting *Quill Corp. v. North Dakota*, 504 U.S. 298, 333 (1992)).

<sup>23</sup> *Id.* at 2100–01 (Gorsuch, J., concurring).

<sup>24</sup> *Id.* at 2087, 2097.

<sup>25</sup> *See id.* at 2100 (Thomas, J., concurring); *id.* at 2100–01 (Gorsuch, J., concurring).

<sup>26</sup> *Id.* at 2101 (Roberts, C.J., dissenting).

presence rule was appropriate for an economy in which electronic commerce is now so prominent.

However, the Chief Justice and his three colleagues joining his *Wayfair* dissent concluded that Congress, not the Court, was the appropriate forum for overturning *Quill*'s rule that a state can impose sales tax collection responsibilities only on a retailer with in-state physical presence.<sup>27</sup> The revision of this rule, the Chief Justice argued, "should be undertaken by Congress."<sup>28</sup>

Congress, he observed, "has in fact been considering whether to alter the rule established in *Bellas Hess* for some time."<sup>29</sup> "[L]egislators may more directly consider the competing interests at stake."<sup>30</sup>

In sum, *Quill* reflected three different perspectives among the Justices of the Court. Four Justices (Chief Justice Roberts and Justices Breyer, Sotomayor, and Kagan) did not dispute the fundamental legitimacy of the dormant Commerce Clause or the unsoundness of the physical presence rule for imposing upon retailers the obligation to collect state sales taxes.<sup>31</sup> However, as a procedural matter, these four dissenting Justices preferred for Congress, rather than the Court, to make any changes to the physical presence rule announced in *Bellas Hess* and confirmed in *Quill*.<sup>32</sup> Three members of the Court (Justices Kennedy, Alito, and Ginsburg) defended the intrinsic validity of the dormant Commerce Clause, but concluded that *Quill* and its physical presence rule were properly overturned by the Court itself.<sup>33</sup> Two Justices (Justices Thomas and Gorsuch) expressed their skepticism about the dormant Commerce Clause and caused *Quill* to be overruled by joining with their three colleagues who, while more positive about the dormant Commerce Clause, supported *Quill*'s demise.<sup>34</sup> Hence, *Wayfair*, by a 5-4 vote, quashed *Quill*.

### III. WYNNE

Similar divisions were evident three years earlier in *Wynne*, another 5-4 dormant Commerce Clause decision.<sup>35</sup> *Wayfair* expanded state authority by abolishing the physical presence rule, thereby permitting states to impose sales tax collection responsibilities on

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<sup>27</sup> *Id.* at 2102 (Roberts, C.J., dissenting).

<sup>28</sup> *Id.* at 2101 (Roberts, C.J., dissenting).

<sup>29</sup> *Id.* at 2102 (Roberts, C.J., dissenting).

<sup>30</sup> *Id.* at 2104 (Roberts, C.J., dissenting).

<sup>31</sup> *See id.* at 2101–05 (Roberts, C.J., dissenting).

<sup>32</sup> *See id.* at 2102–04 (Roberts, C.J., dissenting).

<sup>33</sup> *Id.* at 2089–90, 2099.

<sup>34</sup> *See id.* at 2100 (Thomas, J., concurring); *id.* at 2100 (Gorsuch, J., concurring).

<sup>35</sup> *Comptroller of the Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1791 (2015).



out-of-state internet and mail-order retailers that lack in-state physical presence.<sup>36</sup> In contrast, *Wynne* curbed state taxing authority by requiring states to grant income tax credits to their residents for the out-of-state income taxes such residents pay.<sup>37</sup>

The tax at issue in *Wynne* was the county income tax imposed by Maryland law.<sup>38</sup> While the Maryland state income tax gave Maryland residents credits for the income taxes such residents paid to other states, Maryland did not extend a similar credit under the Maryland county income tax for out-of-state taxes paid by Maryland residents.<sup>39</sup> For a five Justice majority, Justice Alito held that this failure to grant residents a county income tax credit for out-of-state taxes discriminated against interstate commerce in violation of the dormant Commerce Clause.<sup>40</sup>

The four central themes of Justice Alito's opinion were the historic provenance of the dormant Commerce Clause, the analogy between a tariff and Maryland's failure to grant Maryland residents a credit under the Maryland county income tax for out-of-state taxes, the evils of double state taxation, and the "internal consistency" test developed under the dormant Commerce Clause.<sup>41</sup> Presaging his agreement with Justice Kennedy in *Wayfair*, Justice Alito in *Wynne* embraced the legitimacy of the dormant Commerce Clause, which "has deep roots."<sup>42</sup> "[A] state tariff," Justice Alito

<sup>36</sup> See *Wayfair*, 138 S. Ct. at 2099.

<sup>37</sup> See *Wynne*, 135 S. Ct. at 1792. As an alternative to providing its residents with income tax credits for out-of-state income taxes, a state can comply with *Wynne*'s nondiscrimination/internal consistency standard by eschewing the taxation of nonresidents' incomes earned within the state. An income tax imposed only on residents passes the test of internal consistency since, if adopted universally, such a tax only taxes income once—assuming that taxpayers are residents in only one state. See *id.* at 1822 (Ginsburg, J., dissenting). This possibility confirms the point made in the text: *Wayfair* expands state tax authority by permitting a state to impose sales tax collection responsibilities on out-of-state internet sellers. In contrast, *Wynne* restricts state tax authority by requiring states to grant credits to their residents for the out-of-state taxes such residents pay or by abandoning the taxation of nonresidents on the income they earn in the state.

<sup>38</sup> *Id.* at 1792. For more background on *Wynne*, see generally Edward A. Zelinsky, *The Enigma of Wynne*, 7 WM. & MARY BUS. L. REV. 797 (2016), which discusses the enigmatic effects of *Wynne* on future dormant Commerce Clause application, and Brannon P. Denning, *The Dormant Commerce Clause Wynnes Won Wins One: Five Takes on Wynne and Direct Marketing Association*, 100 MINN. L. REV. HEADNOTES 103 (2016), which compares *Wynne* to prior case law to help define its scope of impact.

<sup>39</sup> *Wynne*, 135 S. Ct. at 1792.

<sup>40</sup> *Id.*

<sup>41</sup> See *id.* at 1794–95, 1802, 1804.

<sup>42</sup> *Id.* at 1794. Dissenting in *Dep't of Revenue of Ky. v. Davis*, 553 U.S. 328, 376 (2008), Justice Alito characterized his position in *Davis* and in *United Haulers Ass'n., Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 356 (2007) as "proceed[ing] . . . on the assumption that the Court's established dormant Commerce Clause precedents should be followed . . ." This statement could be interpreted as leaving the door open to a reassessment of the Court's dormant Commerce Clause case law. However, Justice Alito's *Wynne* opinion and

wrote, was “the quintessential evil targeted by the dormant Commerce Clause.”<sup>43</sup> Maryland’s failure to grant residents a credit for out-of-state taxes “has the same economic effect” as a tariff.<sup>44</sup>

Maryland’s county income tax flouts the norms of the dormant Commerce Clause, Justice Alito wrote, because “Maryland’s tax scheme is inherently discriminatory and operates as a tariff.”<sup>45</sup> To advance this characterization, Justice Alito contrasted two hypothetical residents of a state which provides no credit for out-of-state taxes.<sup>46</sup> In this example, one of these residents earns all of her income in-state while the other resident earns his income out-of-state.<sup>47</sup> Because the state in which they live provides no credit for out-of-state taxes, the latter resident pays two state income taxes on his income, one tax to the state of his residence and a second tax to the state in which he earns his income.<sup>48</sup> On the other hand, the first resident pays a single state tax on her income since she earns all of her income in-state.<sup>49</sup> Like a tariff, this encourages residents to generate income at home rather than out-of-state so as to be taxed only once by the state of residence, rather than twice by the state of residence and simultaneously by the second state in which the income is earned.<sup>50</sup>

According to Justice Alito, a state tax scheme which provides no credit for the out-of-state taxes paid by residents violated the dormant Commerce Clause’s internal consistency test.<sup>51</sup> Under this test, the relevant inquiry is what would happen if all states adopted the tax being challenged under the dormant Commerce Clause.<sup>52</sup> Justice Alito answered that in such a theoretical world there are effectively state tariffs nationwide so an individual who ventures to earn out-of-state income in this hypothetical setting is always double taxed by the two states in which she lives and works.<sup>53</sup> In contrast, an individual who just earns income in her home state is taxed only once by her state of residence.<sup>54</sup> This, Justice Alito observed, unconstitutionally discriminates against interstate economic activity.

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his support for Justice Kennedy’s *Wayfair* opinion evince a stronger commitment to the dormant Commerce Clause.

<sup>43</sup> *Wynne*, 135 S. Ct. at 1792.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.* at 1804.

<sup>46</sup> *Id.* at 1803–04.

<sup>47</sup> *Id.* at 1803.

<sup>48</sup> *Id.* at 1803–04.

<sup>49</sup> *Id.* at 1804.

<sup>50</sup> *See id.*

<sup>51</sup> *Id.* at 1803.

<sup>52</sup> *See id.* at 1802.

<sup>53</sup> *Id.* at 1804.

<sup>54</sup> *Id.* at 1803–04.

For himself and Justice Thomas, Justice Scalia in *Wynne* excoriated the dormant Commerce Clause as “a judge-invented rule”<sup>55</sup> which contrasts with “the real Commerce Clause.”<sup>56</sup> The Commerce Clause, Justice Scalia informed us, is an affirmative grant of power to Congress, not a license for judges “to set aside state laws *they believe* burden commerce.”<sup>57</sup> Justice Scalia’s skepticism of the dormant Commerce Clause led him to conclude that, “[f]or reasons of *stare decisis*,”<sup>58</sup> he would strike taxes under the dormant Commerce Clause in only two cases: a state tax which “discriminates on its face against interstate commerce or [a tax which] cannot be distinguished from a tax [the] Court has already held unconstitutional.”<sup>59</sup> In contrast, Justice Thomas was (and is) unwilling to defer to existing dormant Commerce Clause case law in these two or in any other cases.<sup>60</sup>

Justice Ginsburg’s *Wynne* dissent, like Justice Alito’s majority opinion, accepts the legitimacy of the dormant Commerce Clause.<sup>61</sup> However, Justice Ginsburg concluded (joined by Justices Scalia and Kagan) that *Wynne* misapplied the dormant Commerce Clause.<sup>62</sup> Since the Wynnes are Maryland residents, Maryland can tax all of their worldwide income. The dormant Commerce Clause, Justice Ginsburg maintained, does not require Maryland as a state of residence to grant Marylanders like the Wynnes a credit for the out-of-state taxes they pay.<sup>63</sup> Such credits for out-of-state taxes may be wise as a matter of policy. But, Justice Ginsburg argued, there are competing concerns which justify states taxing their residents’ incomes without granting credits for the out-of-state taxes such residents pay: “More is given to the residents of a [s]tate than to those who reside elsewhere, therefore more may be demanded of them.”<sup>64</sup>

Moreover, Maryland residents do not need dormant Commerce Clause protection from their own state’s tax laws since they vote for the legislators and governors who tax them. In contrast, nonresidents need dormant Commerce Clause succor as they do not vote in the state which taxes them on the income they earn in the taxing state.<sup>65</sup> The majority in *Wynne*, Justice Ginsburg argued,

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<sup>55</sup> *Id.* at 1807 (Scalia, J., dissenting).

<sup>56</sup> *Id.* at 1808 (Scalia, J., dissenting).

<sup>57</sup> *Id.* (Scalia, J., dissenting).

<sup>58</sup> *Id.* at 1811 (Scalia, J., dissenting).

<sup>59</sup> *Id.* (Scalia, J., dissenting).

<sup>60</sup> *Id.* (Thomas, J., dissenting).

<sup>61</sup> *See id.* at 1815 (Ginsburg, J., dissenting).

<sup>62</sup> *See id.* at 1814 (Ginsburg, J., dissenting).

<sup>63</sup> *See id.* at 1816 (Ginsburg, J., dissenting).

<sup>64</sup> *Id.* at 1814 (Ginsburg, J., dissenting).

<sup>65</sup> *See id.* at 1814–15 (Ginsburg, J., dissenting).

erroneously constitutionalized “tax policy” better left to “state legislatures and the Congress.”<sup>66</sup>

#### IV. THE FUTURE OF DORMANT COMMERCE CLAUSE SKEPTICISM

An important takeaway from comparing *Wynne* and *Wayfair* is that the Justices who would abolish the dormant Commerce Clause are not close to constituting a majority of the Court. However, in particular cases, these dormant Commerce Clause skeptics can exercise critical influence on the Court’s decisions.

In *Wynne*, it was Justices Scalia and Thomas who scorned the dormant Commerce Clause.<sup>67</sup> In *Wayfair*, Justices Thomas and Gorsuch played the role of dormant Commerce Clause skeptics.<sup>68</sup> In *Wynne*, Justices Scalia and Thomas had no impact on the outcome of the case since five Justices concluded without them that the dormant Commerce Clause requires Maryland to provide a credit under its county income tax to Maryland residents for the out-of-state taxes such residents pay.<sup>69</sup> On the other hand, in *Wayfair*, Justices Thomas and Gorsuch proved critical to the Court’s outcome, giving Justice Kennedy the fourth and fifth votes he needed to overturn *Quill*.<sup>70</sup>

Two uncertainties complicate this situation for the future. First, we do not know whether Justice Kennedy’s successor, Justice Brett Kavanaugh, will share Justice Kennedy’s commitment to the dormant Commerce Clause or whether he will align himself with dormant Commerce Clause skepticism. Second, that skepticism, *Wynne* and *Wayfair* make clear, can come in different forms. Despite his doubts about the dormant Commerce Clause, Justice Scalia remained willing to strike taxes under that doctrine in either of two contexts: When, as a matter of stare decisis, a pending case was clearly controlled by a prior decision, or when discrimination against interstate commerce was apparent “on [the] face” of the challenged state tax.<sup>71</sup> An interesting possibility is that, had Justice Scalia lived, he might, in the interests of stare decisis, have provided Chief Justice Roberts with the fifth *Wayfair* vote for retaining *Quill*.

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<sup>66</sup> See *id.* at 1823 (Ginsburg, J., dissenting).

<sup>67</sup> See *id.* at 1808 (Scalia, J., dissenting).

<sup>68</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2100 (2018) (Thomas, J., concurring); *id.* at 2100 (Gorsuch, J., concurring).

<sup>69</sup> See *Wynne*, 135 S. Ct. at 1791.

<sup>70</sup> See *Wayfair*, 138 S. Ct. at 2087.

<sup>71</sup> *Wynne*, 135 S. Ct. at 1811 (Scalia, J., dissenting).

Justice Thomas, by contrast, will in all cases refuse to apply the dormant Commerce Clause.<sup>72</sup> Justice Gorsuch's brief comments in his *Wayfair* concurrence<sup>73</sup> leave open for him either of these approaches and perhaps others.

In short, the dormant Commerce Clause enjoys broad support among the Justices currently serving on the Court. However, in particular instances, the Justices who are dormant Commerce Clause skeptics may play a pivotal role.<sup>74</sup> *Wayfair* was such a case.<sup>75</sup>

#### V. DOES *WAYFAIR* OPEN THE FLOODGATES?

Whenever the Court overrules a prominent precedent, the question arises: What is next? *Wayfair* makes clear that, in the dormant Commerce Clause context, the answer is: Not much. *Wayfair* does not open the floodgates to revision of the Court's dormant Commerce Clause case law.

This conclusion starts with the four Justices who would have left *Quill* standing despite the admitted unsuitability of the physical presence rule in a world of electronic commerce.<sup>76</sup> Since the Court's dormant Commerce Clause decisions can be revised or rejected by Congress, Chief Justice Roberts and his dissenting colleagues contended, the Court should let the Legislative Branch make whatever changes are required to overturn or modify the Court's dormant Commerce Clause case law.<sup>77</sup>

Moreover, Justice Kennedy made clear that he viewed the judicial overruling of *Quill* as uniquely compelling: "Though *Quill* was wrong on its own terms when it was decided in 1992, since then the Internet revolution has made its earlier error all the more egregious and harmful."<sup>78</sup>

This is not an invitation for the Court to engage in wholesale revision of its dormant Commerce Clause case law. To the contrary, if it requires something on the order of "the Internet revolution" to justify overruling a dormant Commerce Clause precedent, such overruling will be rare.

Only Justice Thomas is committed to a thoroughgoing repudiation of the Court's dormant Commerce Clause oeuvre.<sup>79</sup>

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<sup>72</sup> See *id.* (Thomas, J., dissenting); *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2100 (2018) (Thomas, J., concurring).

<sup>73</sup> *Wayfair*, 138 S. Ct. at 2100 (Gorsuch, J., concurring).

<sup>74</sup> See *id.* at 2087.

<sup>75</sup> See *id.*

<sup>76</sup> See *id.* at 2101–05 (Roberts, C.J., dissenting). Chief Justice Roberts was joined by Justices Breyer, Sotomayor, and Kagan. See *id.*

<sup>77</sup> *Id.* at 2102 (Roberts, C.J., dissenting).

<sup>78</sup> *Id.* at 2097.

<sup>79</sup> See *id.* at 2100 (Thomas, J., concurring).

As just noted, Justice Gorsuch's views are still unarticulated and Justice Kavanaugh, who replaced Justice Kennedy, may or may not be a dormant Commerce Clause skeptic. But even a dormant Commerce Clause skeptic can, like Justice Scalia, temper his opposition to the dormant Commerce Clause with a commitment to stare decisis.<sup>80</sup>

Consider in this context Justice Kagan's positions in *Wayfair* and *Wynne*. In *Wayfair*, Justice Kagan joined the Chief Justice in contending that it was better for Congress, rather than the Court, to overturn or modify the physical presence rule confirmed in *Quill*.<sup>81</sup> In *Wynne*, Justice Kagan joined Justice Ginsburg's dissent which argued, *inter alia*, that Mr. and Mrs. Wynne needed no relief from the Court.<sup>82</sup> As Maryland voters, the Wynnes had recourse to Maryland's political process to relieve them of their double taxation under the Maryland county income tax. Strong deference to political processes, as manifested by Justice Kagan's positions in *Wynne* and *Wayfair*, counsels equally strong respect for precedent since such deference consigns the task of revising dormant Commerce Clause doctrine to the political institutions of government.<sup>83</sup>

## VI. TWO ISSUES FOR THE FUTURE

### A. The Double Taxation of Dual Residents

What are the implications of *Wynne* and *Wayfair* for particular issues the Court is likely to confront in the future? An important dormant Commerce Clause issue going forward is the double taxation of dual state residents.<sup>84</sup> In an earlier age, it was mainly very wealthy individuals whose peripatetic lifestyles caused two or more states to classify them as residents. When two (or more) states levying personal income taxes both assert that the same individual is a resident, this dual resident can be double taxed as both of these states claim the right to tax him on his worldwide income.<sup>85</sup> The double taxation of dual residents is, in practice, particularly pronounced as to a dual resident's

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<sup>80</sup> See *Comptroller of the Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1811 (2015) (Scalia, J., dissenting).

<sup>81</sup> See *Wayfair*, 138 S. Ct. at 2101–02 (Roberts, C.J., dissenting).

<sup>82</sup> See *Wynne*, 135 S. Ct. at 1816, 1823 (Ginsburg, J., dissenting).

<sup>83</sup> See *id.* at 1823 (Ginsburg, J., dissenting); *Wayfair*, 138 S. Ct. at 2101–02 (Roberts, C.J., dissenting).

<sup>84</sup> See Edward A. Zelinsky, *Double Taxing Dual Residents: A Response to Knoll and Mason*, 86 ST. TAX NOTES 677, 677 (2017) [hereinafter *Double Taxing*]; Edward A. Zelinsky, *Apportioning State Personal Income Taxes to Eliminate the Double Taxation of Dual Residents: Thoughts Provoked by the Proposed Minnesota Snowbird Tax*, 15 FLA. TAX REV. 533, 534 (2014) [hereinafter *Apportioning*].

<sup>85</sup> See Zelinsky, *Apportioning*, *supra* note 84, at 536.



retirement income (taxed by both states claiming to be a state of residence)<sup>86</sup> and as to a dual resident's passive investment income, such as dividends and interests (similarly taxed by both states claiming to be this individual's state of residence).<sup>87</sup>

In the contemporary world, the phenomenon of dual state residence has spread to two career families maintaining residences in different states to accommodate both careers.<sup>88</sup> Dual state residence has also spread to "mass affluent" retirees who divide the year between different homes in different states. In these (and other) contexts, an individual spends part of the year living in two different states and thus can be income taxed as a resident by both of them.

It would be best for Congress to eliminate by federal legislation the double state income taxation of dual state residents, or for the states themselves to abate the problem of double taxed dual residents. Absent a political solution enacted by Congress or negotiated among the states, the courts will find themselves implored to grant relief from dual residents' double state income taxation under the dormant Commerce Clause.<sup>89</sup>

I favor a political solution to the problem of double taxed dual residents, either through federal legislation or through formal or informal arrangements among the states. If there is to be a judicial resolution of this issue, the dormant Commerce Clause principle of apportionment is the most compelling of the tools the courts can employ to eliminate the double taxation of dual residents.<sup>90</sup> Others think that the dormant Commerce Clause concept of nondiscrimination, and *Wynne* in particular, are the appropriate doctrinal handles for convincing the courts to bar double taxation of dual residents.<sup>91</sup>

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<sup>86</sup> 4 U.S.C. § 114(a) (2006) ("No State may impose an income tax on any retirement income of an individual who is not a resident or domiciliary of such State (as determined under the laws of such State).").

<sup>87</sup> On the principle that intangible investment-based income is taxed by the taxpayer's state(s) of residence and the double state taxation of such income when an individual is a resident for tax purposes of two states, see Zelinsky, *Apportioning*, *supra* note 84, at 541, 548–49, which discusses the principle of *mobilia sequuntur personam*.

<sup>88</sup> Sue Shellenbarger, *Work & Family: Marriage From a Distance—More couples are living apart—here's what it takes to keep the relationship healthy*, WALL ST. J., Aug. 15, 2018, at A11 ("[O]f married people living apart . . . a sizable number do this for work.").

<sup>89</sup> See, e.g., *Edelman v. New York State Dep't of Taxation & Fin.*, 80 N.Y.S.3d 241, 243 (App. Div. 2018); Edward A. Zelinsky, *The Noto decision and the double state income taxation of dual residents*, OUPBLOG (June 2, 2014), <https://blog.oup.com/2014/06/noto-decision-double-state-income-taxation/> [<http://perma.cc/TN5P-YEAJ>].

<sup>90</sup> Zelinsky, *Double Taxing*, *supra* note 84, at 678; Zelinsky, *Apportioning*, *supra* note 84, at 570.

<sup>91</sup> See generally Michael S. Knoll & Ruth Mason, *New York's Unconstitutional Tax Residence Rule*, 85 ST. TAX NOTES 707 (2017).

*Wynne* indeed reflects a strong aversion to double taxation. But, as we have just seen, *Wynne* and *Wayfair* also reflect commitments by members of the Court to stare decisis and to deference to the political process.<sup>92</sup> Moreover, the Court has in the past condoned the double state taxation of dual residents.<sup>93</sup> *Wynne* and *Wayfair* suggest that the Court will be reluctant to construe the dormant Commerce Clause to forbid the double state income taxation of dual residents since this would entail the Court's repudiation of long-standing case law condoning such double taxation.<sup>94</sup>

Justice Kavanaugh, Justice Kennedy's successor, could play a pivotal role in this area. If Justice Kavanaugh is a dormant Commerce Clause skeptic, it will require near unanimity by the other six Justices of the Court to apply the dormant Commerce Clause to bar the double taxation of dual residents. Even if Justice Kavanaugh adheres to the dormant Commerce Clause, with Justices Thomas and Gorsuch both leery of the dormant Commerce Clause, it will require a strong consensus among the other seven Justices to declare the double taxation of dual residents unconstitutional. *Wynne* and *Wayfair*, both decided 5-4, indicate that strong consensus is not easily achieved today in the dormant Commerce Clause context.<sup>95</sup>

A counterargument is that the Court's decisions permitting the double taxation of dual residents—*Cory v. White*<sup>96</sup> and *Worcester County Trust Co. v. Riley*<sup>97</sup>—were decided under the Due Process Clause. Moreover, these cases involved state-imposed death taxes, rather than state income taxes. The Court could now possibly hold that the double taxation of dual residents is forbidden by the dormant Commerce Clause even though, per these earlier cases, a double state taxation is permitted as a matter of due process. Justice Alito did something similar in *Wynne* when he and four other Justices held that although the Due Process Clause permits states to tax all of their residents' worldwide incomes, the dormant Commerce Clause does not.<sup>98</sup>

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<sup>92</sup> See *Comptroller of the Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1811 (2015) (Scalia, J., dissenting).

<sup>93</sup> *Cory v. White*, 457 U.S. 85, 89 (1982); *Worcester Cty. Tr. Co. v. Riley*, 302 U.S. 292, 298 (1937).

<sup>94</sup> See *Wynne*, 135 S. Ct. at 1811 (Scalia, J., dissenting); *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2101–02 (2018) (Roberts, C.J., dissenting); see also *Worcester Cty. Tr. Co.*, 302 U.S. at 299.

<sup>95</sup> *Wayfair*, 138 S. Ct. at 2087; *Wynne*, 135 S. Ct. at 1791.

<sup>96</sup> 457 U.S. at 89.

<sup>97</sup> 302 U.S. at 292.

<sup>98</sup> *Wynne*, 135 S. Ct. at 1798–99.

Alternatively, the Court could conceivably cabin *Cory* and *Worcester County Trust Co.* to their particular facts (i.e., the double state taxation of dual residents' estates on their deaths).<sup>99</sup>

Moreover, the political process analysis is more ambiguous in the dual resident context than it was in *Wynne*. That ambiguity provides a stronger rationale for the judicial protection of statutory residents since these double-taxed individuals do not vote in the second state assessing the resident-based income tax against them. As Justice Ginsburg observed in *Wynne*,<sup>100</sup> the Wynnes sought tax relief from Maryland where they resided and voted.<sup>101</sup> Double-taxed dual residents are deemed to reside in two states but can vote in only one of them.

Much dual resident taxation is caused by “statutory residence” laws<sup>102</sup> which classify individuals who spend time in a state without being domiciled there as residents for state income tax purposes. A dual state resident will typically vote in the state of her domicile, thus leaving her without the vote in the state of statutory residence which imposes a second, residence-based income tax upon her.<sup>103</sup>

Even if two states both claim to be an individual's state of domicile, it is not likely that the individual can or should vote in both states. And when someone is a statutory resident of two states, he may vote in neither state because his state of domicile is a third state.

In the typical dual resident/double taxation situation, an individual is domiciled in and can vote in only one of the two states taxing her. This is different than the case of the Wynnes—who voted in and were taxed by Maryland—since a double taxed dual resident lacks the ability to vote in at least one of the states taxing her as a resident.

Voting of course is not the only form of political voice. A statutory resident can make political contributions in her state of statutory residence even if she cannot vote in that state because she is not domiciled there. Nevertheless, the political process concerns advanced by Justice Ginsburg in *Wynne*—the Wynnes were Maryland voters<sup>104</sup>—do not carry over to the double taxed dual resident who does not vote in her state of statutory

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<sup>99</sup> See *Cory*, 457 U.S. at 86; *Worcester Cty. Tr. Co.*, 302 U.S. at 294.

<sup>100</sup> *Wynne*, 135 S. Ct. at 1813–15 (Ginsburg, J., dissenting).

<sup>101</sup> *Id.* at 1814–15 (Ginsburg, J., dissenting).

<sup>102</sup> Edward A. Zelinsky, *Defining Residence for Income Tax Purposes: Domicile as Gap-Filler, Citizenship as Proxy and Gap-Filler*, 38 MICH. J. INT'L L. 271, 274–75 (2017); Zelinsky, *Apportioning*, *supra* note 84, at 541–45.

<sup>103</sup> See, e.g., S.C. CODE ANN. § 7-1-25(A) (2011) (stating that for voting purposes, “[a] person's residence is his domicile”).

<sup>104</sup> *Wynne*, 135 S. Ct. at 1814–15 (Ginsburg, J., dissenting).

residence. Moreover, unlike the subject of internet sales taxation, which was a topic of substantial congressional debate,<sup>105</sup> Congress has given virtually no attention to the problem of double taxed dual state residents.

Considering the counterarguments, *Wayfair* and *Wynne*, on balance, indicate that those favoring the Court's intervention to stop the double state income taxation of dual residents face an uphill fight. Long-standing precedents approve double taxation when two states both claim to be the taxpayer's home state for tax purposes.<sup>106</sup> In certain contexts, some Justices conclude that individuals with political remedies do not need the protection of the dormant Commerce Clause.<sup>107</sup> Dual residents typically vote in the state of domicile, which is one of the states taxing them on their worldwide incomes. The Justices who are dormant Commerce Clause skeptics will not extend that doctrine to protect double-taxed dual residents. Consequently, those trying to convince the Court to stop such double taxation via the dormant Commerce Clause face a daunting challenge.

## B. Sourcing Nonresidents' Incomes: The Case of Employer Convenience

A second important dormant Commerce Clause issue for the future is the proper apportionment of individuals' nonresident incomes for those who work in multiple states. Like the sales tax controversy in *Wayfair*, this issue involves the adaption of older legal doctrines to the imperatives of modern technology. Particularly salient in this context is New York's so-called "convenience of the employer" test which has been used by the Empire State to tax nonresident telecommuters on the income they earn while working at their out-of-state homes.<sup>108</sup>

As Justice Ginsburg observed in her *Wynne* dissent, the states' jurisdiction to tax individual incomes rests on the concepts of residence and source.<sup>109</sup> A state of residence can exercise a form of *in personam* jurisdiction over an individual and, on that basis, can tax his entire worldwide income.<sup>110</sup> In contrast, a state of source can tax a nonresident's income on an *in rem* basis, that is, because the income arises within the state even though the nonresident/taxpayer does not live there.

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<sup>105</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2087, 2102 (2018) (Roberts, C.J., dissenting); see also *Zelinsky*, *supra* note 12, at 1189, 1197–98.

<sup>106</sup> See *Cory v. White*, 457 U.S. 85, 89 (1982).

<sup>107</sup> See *Wynne*, 135 S. Ct. at 1813–17 (Ginsburg, J., dissenting).

<sup>108</sup> See *Zelinsky*, *supra* note 7, at 1.

<sup>109</sup> *Wynne*, 135 S. Ct. at 1813–17 (Ginsburg, J., dissenting).

<sup>110</sup> *Id.* at 1814.

Source-based jurisdiction is limited to the income a nonresident earns within the taxing state.

In *Wynne*, Maryland taxed all of the Wynnes' income since the Wynnes were Maryland residents.<sup>111</sup> Many other states also taxed the income the Wynnes earned within those states since those states were the geographic settings within which the Wynnes earned such income.<sup>112</sup> In *Wynne*, there was no difficulty deciding which income was earned in which state of source.

However, modern technology often makes the source of income a contested question. In particular, modern technology permits what is sometimes labeled “telecommuting,” in which an individual works from home for an employer located in another state.<sup>113</sup> Nonresident states can be overly-aggressive in asserting their ability to tax income on the basis of alleged source-based jurisdiction. New York’s “convenience of the employer” doctrine is the paradigmatic instance of such overreaching.<sup>114</sup>

Consider a law professor who lives in Connecticut and teaches in New York.<sup>115</sup> On some days, he commutes to New York where he teaches classes and meets with students and colleagues.<sup>116</sup> On the other days of the week, he works at home doing research and scholarship as well as grading papers and exams. Modern technology facilitates these work-at-home days, by giving the professor access to legal databases for his research and by allowing him to stay in touch with his students and colleagues through email or other electronic forms of communication.

Connecticut taxes all of this professor’s income on the ground that he is a Connecticut resident.<sup>117</sup> New York also taxes all of this nonresident professor’s income on the theory that the

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<sup>111</sup> *Id.* at 1793.

<sup>112</sup> *See id.*

<sup>113</sup> Andrea Loubier, *Benefits of Telecommuting for the Future of Work*, FORBES (July 20, 2017, 11:58 AM), <https://www.forbes.com/sites/andrealoubier/2017/07/20/benefits-of-telecommuting-for-the-future-of-work/#7aecd0c516c6> [<http://perma.cc/P5DB-5H4W>].

<sup>114</sup> Edward A. Zelinsky, *Pass the Multi-State Worker Act Also*, 80 ST. TAX NOTES 719, 720 (2016); Morgan L. Holcomb, *Tax My Ride: Taxing Commuters in our National Economy*, 8 FLA. TAX REV. 885, 922 (2008).

<sup>115</sup> *See In re Zelinsky v. Tax Appeals Tribunal*, 801 N.E.2d 840, 843–44 (N.Y. 2003). On *Zelinsky*, telecommuting, and New York’s “convenience of the employer” rule, see WALTER HELLERSTEIN ET AL., STATE AND LOCAL TAXATION: CASES AND MATERIALS 399–401 (10th ed. 2014).

<sup>116</sup> *See Zelinsky*, 801 N.E.2d at 843–44.

<sup>117</sup> *See* CONN. GEN. STAT. § 12-701(a)(8) (2018) (“Connecticut taxable income of a resident’ means the Connecticut adjusted gross income of a natural person . . . .”); CONN. GEN. STAT. § 12-701(a)(20) (2018) (“Connecticut adjusted gross income’ means adjusted gross income . . . .”).

professor's days worked at home in Connecticut are not for the employer's convenience but are for the professor's lifestyle.<sup>118</sup>

Connecticut gives a credit against its income taxes for the New York taxes the professor pays with respect to the income allocable to the days he teaches in New York.<sup>119</sup> However, Connecticut (like most other states) will not grant a credit for the taxes New York assesses on the days the professor works at home in Connecticut, researching, writing, and grading.<sup>120</sup>

The net result is double taxation of the portion of the professor's income allocable to the days he works at home in Connecticut. New York taxes this nonresident income even though, on these days, the professor, a Connecticut resident, works at home and receives his public services from the Nutmeg State. Connecticut taxes all of the professor's income, grants a credit for the New York taxes allocable to the professor's days spent in New York, but grants no credit for the New York taxes attributable to the income earned on the professor's days working at home in Connecticut.<sup>121</sup>

*Central Greyhound Lines v. Mealey*,<sup>122</sup> critical to Justice Alito's opinion in *Wynne*,<sup>123</sup> indicates that under the dormant Commerce Clause New York cannot tax income earned outside its borders—such as the income the professor is paid for researching, writing, and grading while at home in Connecticut.<sup>124</sup> A nonresident telecommuter working at his out-of-state home is analogous to the bus in *Central Greyhound*, not taxable by the Empire State while the bus traversed the roads of Pennsylvania and New Jersey.<sup>125</sup>

Given the rise of work patterns denoted as telecommuting, the Court should address the import of *Central Greyhound* and the dormant Commerce Clause concept of apportionment in a world of telecommuting. States should only tax nonresidents on income they earn within the state, not income residents earn when they work at their out-of-state homes. Critical to this conclusion is the dormant Commerce Clause concept the Court has called “external consistency,” i.e., that state tax policies

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<sup>118</sup> See *Zelinsky*, 801 N.E.2d at 844–45, 848.

<sup>119</sup> See CONN. GEN. STAT. § 12-704(a)(1) (2018).

<sup>120</sup> See *Zelinsky*, 801 N.E.2d at 849 (“[I]t is Connecticut's refusal to provide a credit to its resident for all of the nonresident income tax that the taxpayer paid to New York that has created the threat of double taxation.”).

<sup>121</sup> *Id.* at 849.

<sup>122</sup> *Cent. Greyhound Lines v. Mealey*, 334 U.S. 653 (1948).

<sup>123</sup> See generally *Comptroller of Treasury of Md. v. Wynne*, 135 S. Ct. 1787 (2015).

<sup>124</sup> See *Cent. Greyhound*, 334 U.S. at 660–63.

<sup>125</sup> See *id.* at 660–64.



must, in practice, apportion their tax bases to reflect accurately where income is earned.<sup>126</sup>

As a counterargument, *Wynne* could be read as requiring Connecticut, as the state of residence, to grant a credit for the New York taxes assessed on this professor's work-at-home days. This, however, is the less persuasive reading of *Wynne*. *Wynne* required Maryland, as the Wynnes' state of residence, to avoid the implicit tariff of double taxation.<sup>127</sup> In particular, *Wynne* held that Maryland's county income "tax unconstitutionally discriminates against interstate commerce" because that tax failed to grant a credit for taxes imposed by other states on the income the Wynnes earned in those other states.<sup>128</sup>

However, Connecticut grants a credit to its residents for the income they earn in New York and other states.<sup>129</sup> Connecticut (like most other states) does not grant credits for taxes imposed by other states on income earned in Connecticut.<sup>130</sup> Thus, the double taxation under New York's so-called "convenience of the employer" doctrine stems, not from the resident state's refusal to grant a credit, but from the nonresident state's refusal to properly apportion and only tax the income earned within its boundaries.

Consequently, the Court's concern about double taxation manifested in *Wynne* should lead to the application of *Central Greyhound* and the external consistency test to the world of telecommuting. States like New York should only tax nonresident individuals on the income they earn in New York, not the income such individuals earn working at their out-of-state homes.

Political process concerns reinforce this conclusion. Like statutory residents, nonresidents do not vote in the states which tax them on a source basis. Aggressive practices, like New York's convenience of the employer doctrine, export New York's tax burdens onto nonvoting, nonresidents. This is an instance of political dysfunction, precisely the situation where the case for applying the dormant Commerce Clause is most compelling.

## VII. CONCLUSION

A comparison of *Wayfair* and *Wynne* indicates that the Court is unlikely to abandon the dormant Commerce Clause altogether. However, the Justices who would forsake the dormant Commerce

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<sup>126</sup> Zelinsky, *supra* note 38, at 808–10 (discussing the future of external consistency after *Wynne*).

<sup>127</sup> *Wynne*, 135 S. Ct. at 1792.

<sup>128</sup> *Id.* at 1797.

<sup>129</sup> See CONN. GEN. STAT. § 12-704(a)(1) (2008).

<sup>130</sup> See *In re Zelinsky v. Tax Appeals Tribunal*, 801 N.E.2d 840, 849 (N.Y. 2003).

Clause can exercise critical influence in specific cases as they did in *Wayfair*.<sup>131</sup> While *Wayfair* overturned *Quill*, *Wayfair* indicates that the Court is reluctant to overrule its dormant Commerce Clause cases.<sup>132</sup> On the other hand, when neither the Court nor Congress has spoken on a particular issue, the Court will consider significant extensions of the dormant Commerce Clause as it did in *Wynne*.<sup>133</sup>

*Wayfair* and *Wynne* suggest that, despite the persuasive arguments against the double state taxation of dual residents' incomes, the Court will be reluctant to overturn its long-standing precedents upholding the double state taxation of dual residents. The Court is more likely to extend dormant Commerce Clause protection when states are overly-aggressive in taxing the incomes of nonresidents such as New York's "convenience of the employer" doctrine.

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<sup>131</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2100 (2018) (Thomas, J., concurring); *id.* at 2100–01 (Gorsuch, J., concurring).

<sup>132</sup> See *id.* at 2102 (Roberts, C.J., dissenting).

<sup>133</sup> See *Wynne*, 135 S. Ct. at 1797.

# Proportionality as Hidden (but Emerging?) Touchstone of American Federalism: Reflections on the *Wayfair* Decision

*Darien Shanske\**

## INTRODUCTION

Until June 2018, a state could not require an out-of-state vendor to collect its use tax if the vendor did not have a physical presence in the state. This was the rule in place during the entire rise of the Internet and of e-vendors such as Amazon, which scrupulously avoided physical presence in as many states as possible. The result was a significant tax advantage for remote vendors as compared to brick and mortar stores, as well as increasing revenue losses for states and localities. It would be one thing if the national legislature had decided to confer this dubious tax advantage, yet this rule emerged not from Congress, but from the Supreme Court.

In *South Dakota v. Wayfair, Inc.*,<sup>1</sup> the Court overturned the physical presence requirement. In so doing the Court did more than just take away an unwise tax advantage that remote vendors did not secure through the political process. The Court also restored the ordinary constitutional balance in two related ways. First, the Court restored the states' power to tax unless Congress has specifically preempted that power. To be sure, the Court has restricted the power of state taxation through application of the dormant Commerce Clause, but modern dormant Commerce Clause doctrine is generally respectful of the background norm that states must be permitted the leeway to raise revenue as they see fit.

Thus, and this is the second restoration, the Court corrected an anomalously formal pocket of dormant Commerce Clause jurisprudence where it had crafted a bright-line rule that also had the effect of reversing the constitutional default in favor of state power.

The exact impact of the *Wayfair* decision on the practice and reality of state and local public finance will take many years to

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<sup>1</sup> 138 S. Ct. 2080 (2018).

emerge. In this Article, I consider *Wayfair* in the context of the Court's federalism jurisprudence. I argue that restoring the constitutional balance helps explain why the case came out as it did. Further, I place the Court's approach to federalism in broader perspective, explaining that it illustrates an apt application of the proportionality principle. The proportionality principle is at the center of constitutional adjudication around the world and explicitly so. I demonstrate that this principle is no less powerful in adjudicating issues arising in our federal system, though typically under some other nominal analytic structure.

## I. HISTORY

First in 1967, and then in 1992, the Court had found that the federal Constitution required the physical presence rule to require an out-of-state vendor to collect use tax for that state.<sup>2</sup> Even in 1967, this was a controversially formal and novel gloss on the Due Process Clause and the dormant Commerce Clause.<sup>3</sup> By 1992, due process jurisprudence had moved so far from formal tests that the physical presence rule seemed to have essentially been overturned, and the North Dakota Supreme Court asserted as much.<sup>4</sup> Getting ahead of the Supreme Court clearly piqued some members of the Court, though there was unanimous agreement that, in fact, the North Dakota Supreme Court was correct as to the Due Process Clause.<sup>5</sup> And thus in 1992, in *Quill*, the Court made it clear that the physical presence rule was not required by the Due Process Clause.<sup>6</sup> Rather, and distinguishing the two clauses in this way for the first time, the Court re-affirmed the physical presence rule, but only as emerging from the dormant Commerce Clause.<sup>7</sup>

Shifting the source of the rule had the seemingly momentous implication that Congress could change the rule if it so chose.<sup>8</sup> Yet over the ensuing twenty-five years Congress did not, though there were numerous proposals to do so. One way of analyzing

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<sup>2</sup> See generally *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill.*, 386 U.S. 753 (1967); *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), *overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>3</sup> See *Bellas Hess*, 386 U.S. at 758. See the powerful dissent written by Justice Fortas on behalf of three Justices. *Id.* at 760 (Fortas, J., dissenting).

<sup>4</sup> See *State ex rel Heitkamp v. Quill Corp.*, 470 N.W.2d 203 (N.D. 1991).

<sup>5</sup> See *Quill*, 504 U.S. at 308.

<sup>6</sup> See *id.* at 305. Interestingly, it is now the Court's due process jurisprudence that leading commentators see as "thinly reasoned," especially in light of *Wayfair*. See Allan Erbsen, *Wayfair Undermines Nicaastro: The Constitutional Connection Between State Tax Authority and Personal Jurisdiction*, 128 YALE L.J.F. (forthcoming 2019), <https://ssrn.com/abstract=3291858>.

<sup>7</sup> See *id.*

<sup>8</sup> See *id.* at 318.

the situation is that Congress was content with the result, perhaps happy that this rule was shielding an infant industry. Alternatively, there is an argument that Congress might have considered overturning *Quill* if only the states had acted to simplify their sales and use tax systems sufficiently.<sup>9</sup>

A counter-narrative argues that Congress, especially the modern Congress, is designed *not* to act and that the states simply could not get quite enough momentum on their side given the determined opposition of remote vendors, states without sales taxes and anti-tax activists.<sup>10</sup> As an empirical matter, Congress seems most likely to act in the interstate context in response to narrow concentrated interests, a finding generally consistent with public choice theory.<sup>11</sup> From this perspective, it would be more likely that Congress would act to shield specific business interests from the states—should the *Quill* rule be removed. We will now have the opportunity to see if this is true, assuming the states overreach somehow.

Given the magnitude of the revenue loss and competitive harm they faced, the states became increasingly creative in asserting nexus even under *Quill*.<sup>12</sup> At the same time, major players, such as Amazon, now found it in their business interest to establish a physical presence in multiple states.<sup>13</sup> Thus, by 2018, the major harm to the states had, to some extent, been mitigated. This situation too could be seen in two ways. On the one hand, one might argue that whatever harm the *Quill* rule had done, it was no longer a pressing problem. On the other hand, one might argue that the *Quill* rule—ostensibly meant to help preserve a uniform market—launched dozens of competing state initiatives to collect the use tax, with more to come as the online market continued to grow in importance.

## II. DECISION

Writing for a 5-4 majority, Justice Kennedy argued that the *Quill* rule was always wrong, and it was not the Court's place to

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<sup>9</sup> This argument was made by the Respondents in *Wayfair*. See Respondents' Brief at 13–17, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494).

<sup>10</sup> I made this argument with a co-author in an amicus brief. See Amicus Curiae Brief of Four U.S. Senators in Support of Petitioner at 20–24, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494).

<sup>11</sup> See Brian Galle, *Congressional Control of State Taxation: Evidence and Lessons for Federalism Theory*, in *THE LAW AND ECONOMICS OF FEDERALISM* 1, 3 (Jonathan Klick ed., 2017).

<sup>12</sup> See Petition for Writ of Certiorari at 12–16, *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), *overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 01-194).

<sup>13</sup> See *Amazon's Physical Presence (Nexus) in States and the Sales Tax Battle*, AM. INDEP. BUS. ALLIANCE (Sep. 27, 2016), <https://www.amiba.net/amazon-nexus-subsidiaries/> [<http://perma.cc/B3VM-C6M6>].

set down an incorrect rule and then wait for Congress to fix it.<sup>14</sup> Going forward, as a matter of doctrine, the majority held that use tax collection obligations can only be imposed if they satisfy three tests. First, the use tax collection obligation must satisfy due process.<sup>15</sup> This was already true in *Quill*.<sup>16</sup> Second, the use tax collection obligation must satisfy the substantial nexus prong of the *Complete Auto* test.<sup>17</sup> This prong no longer requires physical presence and we know that the South Dakota statute at issue satisfies this test.

A state use tax collection requirement must also pass *Pike* balancing. This issue was remanded to the South Dakota courts to consider, though the Court strongly suggested that the South Dakota statute would survive, explaining that:

First, the Act applies a safe harbor to those who transact only limited business in South Dakota. Second, the Act ensures that no obligation to remit the sales tax may be applied retroactively. S.B. 106, § 5. Third, South Dakota is one of more than [twenty] States that have adopted the Streamlined Sales and Use Tax Agreement. This system standardizes taxes to reduce administrative and compliance costs: It requires a single, state level tax administration, uniform definitions of products and services, simplified tax rate structures, and other uniform rules. It also provides sellers access to sales tax administration software paid for by the State. Sellers who choose to use such software are immune from audit liability.<sup>18</sup>

### III. THE RISE OF *PIKE* BALANCING

In hindsight, the application of *Pike* balancing seems obvious. After all, we all learn in *Constitutional Law I* that this is the test we apply to a facially neutral law that arguably nevertheless imposes too great a burden on interstate commerce. Surely this was the heart of the claim made by remote vendors who have constantly reminded the Court of how many thousands of different sales tax jurisdictions there are in this country.

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<sup>14</sup> See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2096–97 (2018).

<sup>15</sup> See *id.* at 2093.

<sup>16</sup> See *id.*

<sup>17</sup> See *id.* at 2099 (“[T]he nexus is clearly sufficient based on both the economic and virtual contacts [R]espondents have with the State. The Act applies only to sellers that deliver more than \$100,000 of goods or services into South Dakota or engage in 200 or more separate transactions for the delivery of goods and services into the State on an annual basis. S.B. 106, § 1. This quantity of business could not have occurred unless the seller availed itself of the substantial privilege of carrying on business in South Dakota. And [R]espondents are large, national companies that undoubtedly maintain an extensive virtual presence.”).

<sup>18</sup> *Id.* at 2099–100.



Nevertheless, *Pike*'s starring role is surprising. Justice Scalia's disdain for *Pike* balancing is well-known,<sup>19</sup> and a great deal of academic commentary supported his basic point that a balancing test is inherently uncertain, policy-driven, and legislative.<sup>20</sup> The Court had not struck down a statute using *Pike* balancing since the 1980s<sup>21</sup> and the consensus seemed to be that the Court would not do so in *Wayfair*.

This was especially true because the Court seemed to use two different rubrics for analyzing taxes versus regulations.<sup>22</sup> Taxes were subjected to the *Complete Auto* test,<sup>23</sup> which does not include *Pike* balancing. However, regulations were subjected to the usual two levels of test: First facial discrimination analysis, second *Pike* balancing.

As evidence of the no-*Pike* consensus, consider that the Petitioner in *Wayfair*—South Dakota—did not raise *Pike* as an alternative test in its petition for certiorari nor in its merit brief. The argument first appears in an amicus brief at the certiorari stage<sup>24</sup> and then in several other amicus briefs, including, notably, that of the Solicitor General.<sup>25</sup> The Respondents, predictably, dismissed *Pike* in their merits brief as “fundamentally unworkable.”<sup>26</sup>

Yet *Pike* arose immediately in oral argument—at the top of page four of the transcript—during Justice Sotomayor's opening questions.<sup>27</sup> Note that Justice Sotomayor seemed to be of the opinion—as was the amici who first emphasized *Pike*—that *Pike*

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19 See, e.g., *Dep't of Revenue of Ky. v. Davis*, 553 U.S. 328, 360 (Scalia, J., concurring). Justice Gorsuch is clearly not a fan either. See, e.g., *Energy & Env't Legal Inst. v. Epel*, 793 F.3d 1169, 1171 (10th Cir. 2015).

20 See, e.g., Brannon P. Denning, *Reconstructing the Dormant Commerce Clause Doctrine*, 50 WM. & MARY L. REV. 417, 453–58 (2008) (listing common critiques).

21 BRANNON P. DENNING, *BITKER ON THE REGULATION OF INTERSTATE AND FOREIGN COMMERCE* 6–33 (2d ed. 2013).

22 Dan T. Coenen, *Where United Haulers Might Take Us: The Future of the State-Self-Promotion Exception to the Dormant Commerce Clause Rule*, 95 IOWA L. REV. 541, 599 (2010); Edward A. Zelinsky, *The False Modesty of Department of Revenue v. Davis: Disrupting the Dormant Commerce Clause Through the Traditional Public Function Doctrine*, 29 VA. TAX REV. 407, 441 (2010).

23 *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977).

24 See Amicus Curiae Brief of Four U.S. Senators in Support of Petitioner, *supra* note 10, at 3.

25 See Brief for the United States as Amicus Curiae Supporting Petitioner, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494), 2018 WL 1168802; see also Brief of Brill et al. as Amici Curiae Supporting Petitioner, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (No. 17-494), 2018 WL 1203457.

26 Respondents' Brief at 57, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (No. 17-494), 2018 WL 1621148.

27 Transcript of Oral Argument at 4–5, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (No. 17-494), 2018 WL 2446095.

should be used *instead* of *Complete Auto*.<sup>28</sup> In *Wayfair*, the Court chose to engage in both the *Complete Auto* and *Pike* analyses.<sup>29</sup>

#### IV. PROPORTIONALITY AS UNDERLYING PRINCIPLE OF HORIZONTAL FEDERALISM

As a matter of constitutional theory, the proportionality principle is the dominant mode around the world for adjudicating claims where there are strong rights-based arguments on both sides.<sup>30</sup> The typical context in which the principle applies occurs when the rights of an individual, say to privacy or due process, clash with the right of the collective, say to freedom from harm.<sup>31</sup> The proportionality principle permits an abridging of individual rights, but only if the collective need is sufficiently important and only to the extent necessary to satisfy that need.

In the context of horizontal federalism, there is also a clash of rights.<sup>32</sup> Indeed, Justice Kennedy, in summarizing dormant Commerce Clause doctrine, explains that its purpose is “to accommodate the necessary balance between state and federal power.”<sup>33</sup> Put in the language of rights, there is the right of subnational governments, here states, to regulate as their citizens think best. But there is also a right of the collective nation not to be overburdened by particular state regulations, as well as the rights of individuals (and businesses) in other states not to be subjected to “foreign” regulations, let alone burdensome ones. As in the case of individual rights, application of the proportionality principle in borderline cases is apt. *Pike* balancing applies this principle, as does the very similar search for sufficiently “substantial nexus.”<sup>34</sup> It is the primary contention of this Article that, however implicit and necessarily messy, the use of proportionality analysis is correct.

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<sup>28</sup> *See id.*

<sup>29</sup> *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2092–93, 2099 (2018).

<sup>30</sup> *See, e.g.,* Bernhard Schlink, *Proportionality in Constitutional Law: Why Everywhere but Here?*, 22 DUKE J. COMP. & INT’L L. 291 (2012) (explaining and comparing balancing and proportionality).

<sup>31</sup> *See, e.g.,* Alec Stone Sweet & Jud Mathews, *Proportionality Balancing and Global Constitutionalism*, 47 COLUM. J. TRANSNAT’L L. 72, 89 (2008); Vicki C. Jackson, *Ambivalent Resistance and Comparative Constitutionalism: Opening Up the Conversation on “Proportionality,”* *Rights and Federalism*, 1 U. PA. J. CONST. L. 583, 626 (1999).

<sup>32</sup> *See* Jackson, *supra* note 31, at 623–34. Jackson’s analysis focuses on the *City of Boerne v. Flores*, 521 U.S. 507 (1997), decision, discussed briefly below.

<sup>33</sup> *Wayfair*, 138 S. Ct. at 2090.

<sup>34</sup> Adam Thimmesch argues, and I agree, that the substantial nexus prong is essentially the same as *Pike* balancing. Adam B. Thimmesch, *A Unifying Approach to Nexus Under the Dormant Commerce Clause*, 116 MICH. L. REV. ONLINE 101, 106 (2018).

V. PROPORTIONALITY IS IN: EXTRATERRITORIALITY IS OUT (AND RIGHTLY SO)<sup>35</sup>

Towards the end of the briefing in *Wayfair*, a doctrine credibly reported as dead<sup>36</sup> made a determined attempt to return from the grave. This doctrine is called the extraterritoriality doctrine, dubbed by then-Judge Gorsuch as “most dormant.”<sup>37</sup> At the margins, this doctrine is unassailable. California cannot impose a regulation on farms in Missouri. It would seem like such a law would fail under any number of constitutional provisions, including not only the Due Process Clause but also the dormant Commerce Clause.

On the other hand, California can clearly regulate the food that is sold in California. The effect of those consumer regulations might well be felt by farmers in Missouri. Does such a regulation have a forbidden extraterritorial effect? The answer based on standard dormant Commerce Clause jurisprudence would be to apply *Pike* balancing. If the California regulation imposed a burden on interstate commerce out of all proportion to the benefit it provides, it would fail.

Yet there is also the extraterritoriality doctrine, which, according to one formulation, requires a court to determine “whether the practical effect of the regulation is to control conduct beyond the boundaries of the State.”<sup>38</sup> Such a test would strike down hundreds of state laws,<sup>39</sup> including presumably use tax collection laws which, of course, are directed at out-of-state vendors. A strong appeal to the extraterritoriality doctrine was made by Paul Clement, a former Solicitor General.<sup>40</sup>

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<sup>35</sup> Note that this section draws from a White Paper on the dormant Commerce Clause that was co-written with Anna Zaret. See generally ANNA ZARET & DARIEN SHANSKE, NAT’L INST. FOR HEALTH POL’Y, THE DORMANT COMMERCE CLAUSE: WHAT IMPACT DOES IT HAVE ON THE REGULATION OF PHARMACEUTICAL COSTS? (2017).

<sup>36</sup> See Brannon P. Denning, *Extraterritoriality and the Dormant Commerce Clause: A Doctrinal Post-Mortem*, 73 LA. L. REV. 979, 1106 (2013).

<sup>37</sup> *Energy & Env’t Legal Inst. v. Epel*, 793 F.3d 1169, 1172 (10th Cir. 2015). Note that Justice Gorsuch refers to this decision in his concurrence in *Wayfair*, as an example of his thinking about the dormant Commerce Clause. See *Wayfair*, 138 S. Ct at 2100–01 (Gorsuch, J., concurring).

<sup>38</sup> *Healy v. The Beer Inst.*, 491 U.S. 324, 336 (1989).

<sup>39</sup> See Jack L. Goldsmith & Alan O. Sykes, *The Internet and the Dormant Commerce Clause*, 110 YALE L.J. 785, 808 (2001); see also Gillian E. Metzger, *Congress, Article IV, and Interstate Relations*, 120 HARV. L. REV. 1468, 1486 (2007); Denning, *supra* note 36, at 1000.

<sup>40</sup> See Brief for Amici Curiae Nat’l Taxpayers Union Found. et al., in Support of Respondents, *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018) (No. 17-494), 2018 WL 1709085, at \*6. Clement likely knew that the extraterritoriality argument was made in *Pharma v. Walsh* on behalf of the Chamber of Commerce by none other than John Roberts, now the Chief Justice. See Brief for the Chamber of Commerce of the United States as Amicus Curiae in Support of Petitioner, *Pharm. Research & Mfrs. of Am. v. Walsh*, 538 U.S. 644 (2003) (No. 01-188), 2002 WL 31120077, at \*15. It is thus all the more striking that the argument got no traction at all in *Wayfair*.

The Court first invalidated a state law for violating the prohibition on extraterritoriality in *Baldwin v. G.A.F. Seelig*.<sup>41</sup> That case involved a New York state law that banned the sale of milk produced out-of-state unless the seller paid a minimum price set by New York when she purchased the milk out-of-state.<sup>42</sup> The unanimous decision said that New York improperly “project[ed] its legislation” beyond its boundaries by dictating the terms of transactions that took place in other states.<sup>43</sup> The most recent application of the doctrine was in *Healy v. The Beer Institute*, where the Court struck down a Connecticut law that required out-of-state beer distributors to affirm that their prices in Connecticut “were and would remain no higher than the lowest prices they would charge for each beer product in the border [s]tates.”<sup>44</sup>

It was in *Healy* where the Court made the sweeping statement that the inquiry is whether “the practical effect of the regulation is to control conduct beyond the boundaries of the State.”<sup>45</sup> Since *Healy*, the Court has not applied the doctrine and, indeed, the doctrine has been criticized because of its potentially vast sweep—sweep inconsistent with federalism values. This point was made in a leading law review article in 2001, and both the Supreme Court and lower courts seem to have taken its lesson to heart by allowing the doctrine to become most dormant.<sup>46</sup>

The leading non-application of the doctrine occurred in *Pharmaceutical Research and Manufacturers of America v. Walsh* in 2003.<sup>47</sup> In that case, Maine enacted a program that encouraged drug manufacturers to enter into rebate agreements with the state.<sup>48</sup> The rebate agreements allowed Maine to provide residents with drugs at discounted prices.<sup>49</sup> To get drug manufacturers to enter the agreements, the state decided to impose Medicaid “prior authorization” procedures on the products of any manufacturer that refused to join the program.<sup>50</sup> The prior authorization procedures generally made the drug less likely to be prescribed and ultimately sold to Medicaid patients. Thus, the state threatened to reduce

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<sup>41</sup> 294 U.S. 511, 519 (1935).

<sup>42</sup> *Id.*

<sup>43</sup> *Id.* at 521.

<sup>44</sup> 491 U.S. 324, 327 (1989).

<sup>45</sup> *Id.* at 336.

<sup>46</sup> See Goldsmith & Sykes, *supra* note 39, at 789–90. For the history and similar analysis, see Denning, *supra* note 36, at 979. The Goldsmith & Sykes article was cited to in the briefing in *Walsh*. Brief of the Nat'l Conference of State Legislatures et al. as Amici Curiae Supporting Respondents, *Pharm. Research & Mfrs. of Am. v. Walsh*, 538 U.S. 644 (No. 01-188), 2002 WL 31506948, at \*23.

<sup>47</sup> *Pharm. Research & Mfrs. of Am. v. Walsh*, 538 U.S. 644, 669 (2003).

<sup>48</sup> *Id.* at 651.

<sup>49</sup> *Id.* at 653–54.

<sup>50</sup> *Id.* at 655.

manufacturer's market share and sales unless it joined the program.<sup>51</sup> The drug manufacturers argued that the law impermissibly regulated out-of-state commerce because it had the inevitable effect of controlling the terms of out-of-state sales between manufacturers and wholesale distributors.<sup>52</sup> Maine argued that the only extraterritorial effect of the law was that it potentially impacted price negotiations between those two parties by reducing the manufacturer's revenue.

The Court unanimously agreed that there was no dormant Commerce Clause violation because the Maine law did not regulate out-of-state transactions, either "by its express terms or its inevitable effect," echoing the conclusion of the First Circuit.<sup>53</sup> Accordingly—as Professor Brandon P. Denning wrote in an article reviewing the rise and fall of the extraterritoriality doctrine—in the modern era extraterritoriality is "for all intents and purposes, dead."<sup>54</sup> However, and returning to where we started, a state that expressly regulates out-of-state conduct directly is a problem. But that is not the kind of law that is typically at issue. For example, the use tax collection laws regulate how an out-of-state vendor must conduct its *in-state* sales.

Therefore, the extraterritoriality doctrine is not even necessary. The problem with the linking laws struck down in the leading extraterritoriality cases can be explained using *Pike* balancing.<sup>55</sup> The problem with linking is that it imposes a significant burden on interstate business, and for little gain. Indeed, the burden could be impossible if every state regulated prices based on every other state's prices.

It is dangerous to draw conclusions from the dog that did not bark of course. Still, it is striking that the formal—and most definitely non-balancing—test of extraterritoriality got no traction, even as *Pike* took center stage.

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<sup>51</sup> *Id.* at 656.

<sup>52</sup> *Id.*

<sup>53</sup> *Id.* at 645.

<sup>54</sup> Denning, *supra* note 36, at 1006.

<sup>55</sup> *Energy & Env't Legal Inst. v. Epel*, 793 F.3d 1169, 1173 (10th Cir. 2015). Indeed, then-Judge Gorsuch and Judge Sutton argued that the extraterritoriality cases also could have been decided on the basis of illicit discrimination. *See also Am. Beverage Assoc. v. Snyder*, 735 F.3d 362, 381 (6th Cir. 2013) (Sutton, J., concurring) (arguing that all cases that apply extraterritoriality to strike down a state law, involved dormant Commerce Clause protectionism concerns).

## VI. PROPORTIONALITY AS UNDERLYING PRINCIPLE OF VERTICAL FEDERALISM

It is worth noting here that the recent leading case on *vertical* federalism (*NFIB v. Sebelius*) also relies on the proportionality principle. In this area, the question is how to balance the legitimate desire of the central government to advance national goals with the ability of the states to choose other goals. The rule here seems to be that the federal government can do quite a lot to encourage states, but not too much. Consider the details of the Court's ruling on the Medicaid expansion in *NFIB v. Sebelius*—the first Obamacare decision.<sup>56</sup> The Court made it clear that the federal government can spend—and not spend—in order to cajole the states to cooperate with it. But the federal government cannot go too far and coerce the states by taking away a major source of funding on which they had come to rely.<sup>57</sup>

And proportionality plays an explicit role in another key vertical federalism decision, *City of Boerne v. Flores*.<sup>58</sup> There the question is how far Congress's power extends under Section 5 of the Fourteenth Amendment.<sup>59</sup> Clearly Congress's enforcement power must extend to protect the rights granted by the Amendment and, yet, those rights are broad and if Congress's enforcement power were also broad, then that would give Congress an enormous amount of power to preempt state law. The Court, in an opinion by Justice Kennedy, resolved the conflict between the need of the central government to enforce national law and that of the states to retain their powers to regulate by crafting a proportionality test: "There must be a congruence and proportionality between the injury to be prevented or remedied and the means adopted to that end."<sup>60</sup>

## VII. ANOTHER QUIET DOG: *MURPHY V. NCAA*

In *Murphy v. NCAA*,<sup>61</sup> a decision authored by Justice Alito, and joined by Chief Justice Roberts and Justices Kennedy, Thomas, Kagan, and Gorsuch, the Court struck down a federal law that made it unlawful for states or their subdivisions to authorize betting on sporting events.<sup>62</sup> The majority thought that this

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<sup>56</sup> 567 U.S. 519 (2012).

<sup>57</sup> For further analysis, see Darien Shanske & David Gamage, *The Federal Government's Power to Restrict State Taxation*, 81 ST. TAX NOTES 547, 550 (2016).

<sup>58</sup> 521 U.S. 507, 512 (1997).

<sup>59</sup> *Id.* at 516–17.

<sup>60</sup> *Id.* at 520.

<sup>61</sup> *Murphy v. Nat'l Collegiate Athletic Ass'n*, 138 S. Ct. 1461 (2018).

<sup>62</sup> *Id.* at 1468.



decision followed from the anti-commandeering principle, namely that “Congress cannot issue direct orders to state legislatures.”<sup>63</sup>

Daniel Hemel has made the strong case that this dicta throws into doubt the many statutes in which Congress tells the states that they may not tax a given transaction or party.<sup>64</sup> After all, in those statutes, Congress is telling state legislatures what they cannot do, and as to a matter inherent to their sovereignty, namely how to raise revenue.

Many commentators replied to Hemel that this cannot be what *Murphy* means, offering various arguments as to how the Court (and in the meantime courts) can follow *Murphy* but not take it so far.<sup>65</sup> Even the Court does not seem to think that *Murphy* implies that Congress cannot preempt state tax legislation, since all nine Justices in *Wayfair* seemed to believe that Congress can (and should) provide uniform ground rules in this area.<sup>66</sup> The structure of such a statute must, out of necessity, forbid state legislatures from passing certain kinds of tax laws.

But what is the underlying *reason* that *Murphy* should not be read in this way? Put another way, I think there are ways to distinguish *Murphy*, but why should we do so? Or rather, why did it seem obvious to the Justices in *Wayfair* that Congress can preempt state taxing power in connection with the use tax no matter the implication of the dicta in *Murphy*? Again, I would argue that it is because the proportionality principle is the proper way to adjudicate clashes of broad constitutional principles.<sup>67</sup> Of course, the national government must be able to exert some control over state taxing power, but that control cannot go too far, or it would undermine the ability of the states to operate as sovereigns.

The restriction on state legislative power struck down in *Murphy*, on this reading, is better understood as the federal government going too far rather than failing a formal test as to who it is commandeering.<sup>68</sup> Consider how Justice Alito chooses to

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<sup>63</sup> *Id.* at 1478.

<sup>64</sup> Daniel Hemel, *More on Murphy—and a Response to Critics*, MEDIUM (May 16, 2016), <https://medium.com/whatever-source-derived/more-on-murphy-and-a-response-to-critics-471b35c75ecb> [http://perma.cc/7YKF-6SZ5].

<sup>65</sup> See, e.g., Rick Hills, *Murphy v. NCAA’s Escape from Baseline Hell*, PRAWFSBLAWG (May 16, 2018, 7:11 PM), <https://prawnsblawg.blogspot.com/prawnsblawg/2018/05/murphy-v-ncaas-escape-from-baseline-hell.html> [http://perma.cc/LYS5-8M99].

<sup>66</sup> See generally *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>67</sup> Brian Galle, for instance, makes a similar argument. See Brian Galle, *Murphy’s (Misguided) Law*, MEDIUM (May 15, 2018), <https://medium.com/whatever-source-derived/murphys-misguided-law-8c22889918e4> [http://perma.cc/9XMD-X75N].

<sup>68</sup> Obviously, as to *Murphy*, this requires reading the opinion against itself. See *Murphy*, 138 S. Ct. at 1485.

develop the facts underlying the case; he starts with: “Americans have never been of one mind about gambling, and attitudes have swung back and forth.”<sup>69</sup> The federal government has thus taken a position on a controversial topic on which there is considerable disagreement and on which there seems to be little imperative for a national solution.

#### VIII. WAYFAIR ITSELF AS A BALANCING DECISION

*Wayfair* was decided 5-4.<sup>70</sup> One might assume that the four dissenters thought that the *Quill* rule should be upheld because *Quill* itself (and *Bellas Hess*) was correctly decided. For instance, the *Quill* rule does arguably provide certainty. Yet, in the end, not a single Justice would stand up for the rule of *Quill*; but then why was this a 5-4 decision?

The four dissenters argued that stare decisis should protect the *Quill* rule—even though it was always a mistake—because it is an old rule that Congress can change.<sup>71</sup> I take the key part of the majority response to be the following:

While it can be conceded that Congress has the authority to change the physical presence rule, Congress cannot change the constitutional default rule. It is inconsistent with the Court’s proper role to ask Congress to address a false constitutional premise of this Court’s own creation. Courts have acted as the front line of review in this limited sphere; and hence it is important that their principles be accurate and logical, whether or not Congress can or will act in response. It is currently the Court, and not Congress, that is limiting the lawful prerogatives of the States.<sup>72</sup>

Put another way, Justice Kennedy is arguing that federalism values establish a pro-state power default and that it is untenable for a federal court, as a court, to erect a barrier to state power based on a mistake.

But note that the dissent’s ode to stare decisis was written by Chief Justice Roberts,<sup>73</sup> who, in another context wrote: “The dormant Commerce Clause is not a roving license for federal courts to decide what activities are appropriate for state and local government to undertake . . . .”<sup>74</sup> The issue in that case, *United Haulers Ass’n., Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, was whether a public utility could force local users to use its waste

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<sup>69</sup> *Id.* at 1468.

<sup>70</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2087 (2018).

<sup>71</sup> *Id.* at 2102 (Roberts, C.J., dissenting).

<sup>72</sup> *Id.* at 2096–97.

<sup>73</sup> *Id.* at 2102.

<sup>74</sup> *United Haulers Ass’n., Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 343 (2007).

treatment services, and Chief Justice Roberts held for the majority that it *could*.<sup>75</sup> Justice Alito wrote a powerful dissent in this case and was joined by Justice Kennedy.<sup>76</sup> Justice Alito again joined Justice Kennedy in *Wayfair*.<sup>77</sup> Thus, according to Justices Alito and Kennedy, a pro-state constitutional default does not protect local flow control ordinances, but does protect the ability of states to impose a use tax collection obligation. Note that one cannot distinguish *Wayfair* from *United Haulers* because of stare decisis, as in both cases there was a precedent on point that had to be overturned in fact (or de facto, as in *United Haulers*).

How do we think through this tangle? Through how the Justices weighed the facts. Consider Chief Justice Roberts. In *United Haulers*, Chief Justice Roberts began his decision explaining why waste treatment was a significant and intractable problem of the sort that he clearly thought it appropriate for local governments to solve.<sup>78</sup> By contrast, in *Wayfair*, Chief Justice Roberts emphasized that the problem of use tax collection had apparently been largely solved and so there was no reason to destabilize matters by changing a flawed rule, especially a rule that Congress could change.<sup>79</sup>

For Justice Alito in *United Haulers* (and Justice Kennedy who signed onto his dissent), opening the door for local governments to force residents to use their services was sure to lead to wave after wave of local protectionist strictures.<sup>80</sup> For Justice Kennedy in *Wayfair* (and Justice Alito who signed on to his majority opinion),<sup>81</sup> the states' struggle to mitigate an incorrect rule while waiting for Congress to act, was itself a significant harm. Justice Kennedy also did not agree that the *Quill* problem had been largely solved.

## IX. CONCLUSION: DON'T FEAR THE SCALES

As it turns out, I think Chief Justice Roberts was correct in *United Haulers* and that Justices Kennedy and Alito were correct in *Wayfair*. What should one make of this dissensus? Does it not indicate that there is no underlying principle, just

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<sup>75</sup> See *id.* at 347.

<sup>76</sup> See *id.* at 355 (Alito, J., dissenting).

<sup>77</sup> *Wayfair*, 138 S. Ct. at 2087.

<sup>78</sup> *United Haulers*, 550 U.S. at 334.

<sup>79</sup> See *Wayfair*, 138 S. Ct. at 2103 (Roberts, C.J., dissenting) (“States and local governments are already able to collect approximately [eighty] percent of the tax revenue that would be available if there were no physical-presence rule.”).

<sup>80</sup> *United Haulers*, 550 U.S. at 364 (Alito, J., dissenting) (“Experience in other countries, where state ownership is more common than it is in this country, teaches that governments often discriminate in favor of state-owned businesses (by shielding them from international competition) precisely for the purpose of protecting those who derive economic benefits from those businesses, including their employees.”).

<sup>81</sup> *Wayfair*, 138 S. Ct. at 2087.

legislative judgments? Or, if there is a principle, don't the different results indicate that the principle is failing to produce the kind of predictable results required by the rule of law? These are big questions, and oft-debated ones. I think considering our little universe of dormant Commerce Clause cases illustrates why one might be—and I am—satisfied with these somewhat unsettled results.

When the Justices engage in proportionality analysis, they are weighing substantial principles that are in conflict. The resulting balance between principles is itself a kind of principle. That is, once a certain judicial balance is chosen, it applies to all states, not just favored ones. All states can impose a use tax collection obligation if they follow South Dakota's lead. All localities can impose a flow control ordinance directing residents to use a publicly-owned facility.

This is not like ordinary legislative balancing. A government needs to set a tax rate or a set of tax rates, and, though this is also an inexact science, it does not necessarily involve a clash of principles. No one has a rights-based claim to be in a particular tax bracket in the abstract. Tax rates reflect a balance of considerations, but typically not a balance of rights of constitutional dimension. Further, once the rates are set, the government can give out—and does give out—tax breaks reducing the taxes of some for narrow policy reasons, even if the reasons are daft (and are truly just political giveaways).

Though proportionality judgments are not merely legislative judgments, the final balancing as to constitutional principles will change with time, and with Justices. Is there not something incongruous about the Court returning to the fray again and again, often with fractured opinions, in order to achieve balance? Not if one recognizes that the balancing is itself a requirement because of the import of the competing imperatives being considered. Adopting a formal rule is ultimately to discount the principle on one side, as the *Quill* rule did violence to the interests of the states.

Since the balancing must itself be a product of judgment, we assess its quality except on the basis of how the balancing is actually done. To some extent, we do not yet know the answer, as many post-*Wayfair* “balancings” await the courts. That said, in upholding the quite reasonable South Dakota statute, the Court has gotten us off to a promising start.<sup>82</sup>

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<sup>82</sup> Hayes Holderness, *Navigating 21st Century Tax Jurisdiction* (Jan. 11, 2019) (unpublished manuscript), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3314272](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3314272).

Even if appropriate for the Court to engage in this kind of balancing in the abstract, what about the weak textual warrant for our courts doing so? The textual warrant of the dormant Commerce Clause is another huge question but note that fact-intensive inquiries analogous to *Pike* balancing are a feature of international trade law—that is to agreements that nations have explicitly negotiated among themselves.<sup>83</sup> This makes sense. Parties to a free trade agreement reasonably desire a backup test should facially non-discriminatory local laws cause a discriminatory effect. Thus, Congress has already acceded to balancing rules in the context of facilitating an international free trade zone. If Congress passed a law about interstate commerce, it would presumably use a similar rubric to police the domestic free trade zone.<sup>84</sup> It would then be up to the Supreme Court to apply that statute and that application would look pretty much exactly like current dormant Commerce Clause cases. The Court's dormant Commerce Clause jurisprudence was thus once prescient and remains necessary. As the *Quill* saga demonstrates, throwing matters back to Congress is a fraught enterprise, even when there is broad consensus as to what should be done. We are stuck with the dormant Commerce Clause.

In sum, *Wayfair* holds that the states may impose a use tax collection obligation on remote vendors, but not if the burden placed upon them is too great because such a burden undermines the national marketplace.<sup>85</sup> How much is too much will be decided via a common law process and that is, I contend, just how it should be and must be. The only problem with the current state of affairs is that the operative analytic principle, namely the proportionality principle, has not been embraced as such by the Court. Given its cosmopolitan provenance, it seems unlikely that such an explicit embrace will come anytime soon.

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<sup>83</sup> See, e.g., Daniel A. Farber & Robert E. Hudec, *Free Trade and the Regulatory State: A GATT's-Eye View of the Dormant Commerce Clause*, 47 VAND. L. REV. 1401, 1421 (1994) (“As is true of DCC doctrine, the GATT law also deals with facially neutral measures that disadvantage foreign firms compared with domestic ones.”).

<sup>84</sup> Indeed, Congress does use the “unreasonable burden” test in narrow interstate contexts. See 49 U.S.C. § 40116(d) (2018).

<sup>85</sup> See *supra* Part II.





# Tax Competition and the Dormant Commerce Clause: A Japanese Perspective

*Keigo Fuchi\**

## INTRODUCTION

Given the vital role the dormant Commerce Clause plays in delineating tax jurisdictions of the states and local governments, it would be difficult to imagine what would happen without this legal doctrine. This Article will show that the absence of a dormant Commerce Clause equivalent in Japan has given rise to serious tax competition. By illustrating the significance of this legal doctrine and the holding in *South Dakota v. Wayfair, Inc.*,<sup>1</sup> this Article demonstrates that Japan could use a similar legal framework of fiscal federalism from a comparative perspective.

Part I traces the historical development of the dormant Commerce Clause jurisprudence with respect to the collection duty for consumption taxes. Particularly, it articulates the rise and fall of four theories on the constitutionality of the collection duty proposed by the Supreme Court Justices in the 1940s. Part I concludes by pointing out that *Wayfair* removes obstacles to achieving ideal state consumption taxes.

Part II starts by briefly describing the Japanese tax system.<sup>2</sup> Japan is not a federal state, and certain statutes regulating local governments (both prefectures and municipalities) secure each governments' autonomy. These statutes grant local governments a qualified power to impose their own "extra-statutory taxes"—taxes that are exclusively based on ordinances [jorei] of a local government. The tax revenue system for local governments in Japan is unique. Property tax and local personal income tax are kept by municipalities as their principal sources of revenue. Local corporate income tax is the most important source of revenue for prefectures. Such division and allocation of the sources of revenue gives rise to a considerable disparity of tax revenue among local governments. This Part illustrates how this disparity gives rise to tax competition among local governments in Japan, highlighting the absence of a Japanese

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<sup>1</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2089–96 (2018).

<sup>2</sup> *See infra* Part II.

dormant Commerce Clause equivalent. The Japanese courts have failed to put forward a meaningful standard to judge whether local tax legislation interferes with, and places an undue burden on, free movement of goods and services within the country. The content of the provisions of the Local Tax Act—the statute governing whether local tax legislation interferes with, and thereby places an undue burden on, the movement of goods and services within Japan—is, to say the least, vague. Moreover, it is not obvious whether clear principles for allocating taxing powers among local governments are truly recognized in Japan. Part II then discusses two examples that highlight the absence of a dormant Commerce Clause equivalent in Japan. First, this Part examines taxation by some local governments that induces the exports of nuclear waste. It is apparent that the tax discriminates against interstate commerce, but there are no means to invalidate the tax. The second is the recent “hometown tax donation” system that makes it possible for a taxpayer to pay a part of his tax to other local governments. Although this system is becoming popular and being praised as an excellent tool for revitalizing local economy in Japan, it conflicts with most of the principles pronounced by the United States Supreme Court. This Article concludes by emphasizing the significance of the dormant Commerce Clause and *Wayfair* and how Japan can learn from United States jurisprudence and its local taxation system.

## I. THE HISTORICAL DEVELOPMENT OF THE DORMANT COMMERCE CLAUSE CASES ON THE COLLECTION DUTY FOR STATE CONSUMPTION TAXES

### A. Introduction

In this Part, this Article discusses the role of the dormant Commerce Clause in limiting the tax sovereignty of the states. Before proceeding to an analysis of the cases, two preliminary comments are worth noting.

First, apart from concrete provisions of the constitution and statutes of each country, the extent of taxing power can be divided into two questions. The first question is whether imposing a given tax to a given person, property, or transaction is within the scope of the tax jurisdiction of the state or local government. When the taxation is deemed to be an extraterritorial exercise of its tax jurisdiction, it is per se unconstitutional or illegal. The second question asks, given that the tax itself is within the government’s jurisdiction, whether the imposition of the tax affects the economic activity and/or the decision-making of people so much that it conflicts with the exercise of the police power of other states or local governments. The exercise of the taxing power by one state

may significantly harm another state's exercise of regulatory power. In this case, the exercise of taxing power will be invalidated. In the United States, throughout the development of case law on state taxation, these two questions are treated concurrently and sometimes inseparably. Both the Due Process Clause and the dormant Commerce Clause are employed for answering the questions.

Second, the nature of the tax or the duty in question is important in determining their validity. Since its birth as a judicial doctrine, the dormant Commerce Clause has often applied to state and local tax cases. One of the most difficult issues has been determining the conditions under which a state can mandate nonresidents or out of state businesses to be subject to state use tax.<sup>3</sup> Here, the consumers of goods and services, to whom the economic burden of the tax shifts, are supposed to be residents of the state. This is a difficult issue because the nature of use tax is equivocal.

To begin with, the state may impose sales tax on businesses as an indirect tax.<sup>4</sup> The taxpayers of the sales tax are the businesses, whereas the economic burden of the tax shifts to the consumers of the goods and services sold. The businesses are located in the state or at least have sufficient factual connection with the jurisdiction. Therefore, nothing prevents the state from imposing sales tax liability on them.

Use tax is, from its inception, a supplementary tax contrived to avoid any possible doubts as to the taxing power against out-of-state businesses. The taxpayers of the use tax are consumers—residents of the state. They also bear the burden of the tax. There is no problem for the state to impose the tax on its residents. However, the key issue is whether it is possible to designate businesses as the agent for collection and payment of the tax. In use tax, the consumers have only secondary liability, even though they are the original taxpayers. Otherwise they would be exempt from the duty. If we take this legal construction at face value, there appears to be no extraterritorial exercise of taxing power. The consumers, the original taxpayers, are within the boundary of the state. It is their agent who was on the outside of the territory by chance. Moreover, it might be argued that the liability of the agent is not tax liability, but a duty to act or cooperate with the state in a certain way.

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<sup>3</sup> See generally *Wayfair*, 138 S. Ct. 2080.

<sup>4</sup> See generally John L. Mikesell, *Remote Vendors and American Sales and Use Taxation: The Balance between Fixing the Problem and Fixing the Tax*, 53 NAT'L TAX J. 1273 (2000) (indicating that retail sales taxes are defensible as the American approach to indirect consumption taxation).

If this is the case, the constitutionality of the duty would be better decided according to non-tax precedent.

However, if we take seriously the fact that use tax is in effect a version of sales tax, we should apply the same legal standards used to analyze sales tax. It follows that the businesses located out-of-state must be regarded not as just a collecting agent, but as the taxpayer of use tax. Thus, it would be almost impossible to justify use tax without also justifying sales tax against out-of-state retailers at the same time.

## B. Early Cases

The earliest case on collection duty and the dormant Commerce Clause was an excise tax case.<sup>5</sup> In *Monamotor Oil Co. v. Johnson*, Iowa imposed a license fee on all motor vehicle fuel used in the state.<sup>6</sup> The Iowa statute required distributors to charge users a price that includes the license fee and to remit license fee proceeds to the state treasurer.<sup>7</sup> The Plaintiff claimed that the statute imposed a burden upon interstate commerce.<sup>8</sup> The Supreme Court, in an opinion delivered by Justice Roberts, rejected that claim holding that the levy “falls on the local use after interstate commerce has ended”<sup>9</sup> and the distributor’s burden is “too slight.”<sup>10</sup>

A few years later, the first case on use tax reached the Supreme Court.<sup>11</sup> In *Felt & Tarrant Mfg. Co. v. Gallagher*, California required retailers that maintained a place of business in the state to collect use tax from purchasers.<sup>12</sup> The Plaintiff, who manufactured and sold “comptometers” in the state through two general agents, claimed that the collection of use tax conflicted with the dormant Commerce Clause and the Due Process Clause.<sup>13</sup> Justice McReynolds’s opinion for the Supreme Court summarily rejected the Plaintiff’s claim without presenting much, if any, reasoning for the Court’s decision.<sup>14</sup>

A Supreme Court decision in 1940, regarding sales tax by New York City (not use tax), articulated the Court’s attitude toward the collection duty of retailers.<sup>15</sup> In a footnote in

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<sup>5</sup> See *Monamotor Oil v. Johnson*, 292 U.S. 86, 93 (1934).

<sup>6</sup> *Id.*

<sup>7</sup> *Id.* at 88–89.

<sup>8</sup> See *id.* at 93.

<sup>9</sup> *Id.*

<sup>10</sup> *Id.* at 94.

<sup>11</sup> See *Felt & Tarrant Mfg. v. Gallagher*, 306 U.S. 62, 64 (1939).

<sup>12</sup> *Id.* at 66.

<sup>13</sup> *Id.* at 64, 66.

<sup>14</sup> See *id.* at 65–66.

<sup>15</sup> See *McGoldrick v. Berwind-White Coal Mining*, 309 U.S. 33 (1940).

*McGoldrick v. Berwind-White Coal Mining Co.*, Justice Stone made clear the duty “does not violate the [C]ommerce [C]lause.”<sup>16</sup> At that time, the question of whether out-of-state businesses’ duty to collect tax was constitutional was not treated separately from the constitutionality of the tax itself. Even though the Court held the duty to collect tax to be lawful in these three cases, it did not offer any material reason for its decisions.

In 1944, two decisions of the Supreme Court were handed down on the same day directly dealing with the collection duty of use tax as well as the related question of territorial limits of taxing power for sales tax.<sup>17</sup> In *McLeod v. J. E. Dilworth Co.*, the issue was whether the levy of sales tax by Arkansas on a Tennessee corporation with no place of business in Arkansas was constitutional.<sup>18</sup> The Court held, in the opinion by Justice Frankfurter, that taxing sales consummated out-of-state “would be to project its powers beyond its boundaries and to tax an interstate transaction.”<sup>19</sup> The Court also emphasized the difference between a sales tax and a use tax. Whereas the former is “a tax on the freedom of purchase,” the latter is “a tax on the enjoyment of that which was purchased.”<sup>20</sup> In *General Trading Co. v. State Tax Comm’n of Iowa*, the issue was whether it was constitutional for Iowa to impose a duty to collect use tax from a Minnesota corporation.<sup>21</sup> Based on the lower court’s finding that the corporation was a “retailer maintaining a place of business in [the] state,” the Supreme Court, in an opinion also delivered by Justice Frankfurter, upheld the Iowa legislation and affirmed the collection duty.<sup>22</sup> In sum, Justice Frankfurter’s opinions distinguished use tax from sales tax and applied a different standard in judging the constitutionality of each.<sup>23</sup> It is worth noting that Justice Frankfurter’s opinions did not refer to the Due Process Clause in either of the cases.<sup>24</sup>

The opinions delivered by Justice Frankfurter garnered concurrences and dissents by other Justices. These concurrences and dissents opened the door to the development of the constitutional doctrines on the collection duty.

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<sup>16</sup> *Id.* at 50 n.9.

<sup>17</sup> See generally *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327 (1944); *Gen. Trading Co. v. State Tax Comm’n of Iowa*, 322 U.S. 335 (1944).

<sup>18</sup> *Dilworth*, 322 U.S. at 328.

<sup>19</sup> *Id.* at 330.

<sup>20</sup> *Id.*

<sup>21</sup> *Gen. Trading Co.*, 322 U.S. at 336.

<sup>22</sup> *Id.* at 337–39.

<sup>23</sup> See *Dilworth*, 322 U.S. at 330; *Gen. Trading Co.*, 322 U.S. at 338.

<sup>24</sup> See generally *Dilworth*, 322 U.S. 327; *Gen. Trading Co.*, 322 U.S. 335.

In his dissenting opinion in *Dilworth*, Justice Douglas criticized the majority opinion for being inconsistent with the Court's precedents.<sup>25</sup> His claim stemmed from the observation that the economic impact of sales tax and use tax are the same.<sup>26</sup> According to Justice Douglas, both sales and use taxes are indirect consumption taxes on the consumer.<sup>27</sup> In his dissent, Justice Douglas opined, "[i]n terms of state power, receipt of goods within the State of the buyer is as adequate a basis for the exercise of the taxing power as use within the State."<sup>28</sup> It follows that as long as imposing use tax does not conflict with the dormant Commerce Clause, levying sales tax does not either.<sup>29</sup> Although Justice Douglas said nothing about the collection duty in his dissent, from his view that sales tax and use tax are one and the same, we can infer that he wanted to see as little difference as possible in the collection process of the two taxes.

Justice Jackson also found an affinity between the two taxes. However, unlike Justice Douglas, Justice Jackson asserted that not only the sales tax in *Dilworth*, but also the use tax in *General Trading Co.*, should be invalidated.<sup>30</sup> In his dissent in *General Trading Co.*, Justice Jackson formulated the issue to be whether a person is within the jurisdiction of a state.<sup>31</sup> He first assumed that the power to make a person a tax collector is the same as the power to tax.<sup>32</sup> It follows that a nonresident who should not be a taxpayer for the purpose of sales tax must not be a tax collector of use tax either.<sup>33</sup> Justice Jackson built his argument on the concept of jurisdiction but did not articulate the legal basis from which the concept was derived.

Justice Rutledge, who would have upheld both the sales tax in *Dilworth* and the use tax in *General Trading Co.*, distinguished the Due Process Clause from the dormant Commerce Clause.<sup>34</sup> He considered the Due Process Clause as placing jurisdictional limitations on tax in general and thus, saw little significance in the name of sales tax or use tax.<sup>35</sup> Rather, Justice Rutledge

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<sup>25</sup> See *Dilworth*, 322 U.S. at 332 (Douglas, J., dissenting).

<sup>26</sup> *Id.* at 332–34 (Douglas, J., dissenting) (indicating that "realistically the sales tax is a tax on the receipt of that which was purchased" and is therefore equivalent to the use tax).

<sup>27</sup> *Id.* at 333 (Douglas, J., dissenting).

<sup>28</sup> *Id.* at 334 (Douglas, J., dissenting).

<sup>29</sup> See *id.* (Douglas, J., dissenting).

<sup>30</sup> See *Gen. Trading Co. v. State Tax Comm'n of Iowa*, 322 U.S. 335, 339–40 (1944) (Jackson, J., dissenting).

<sup>31</sup> *Id.* at 339 (Jackson, J., dissenting).

<sup>32</sup> See *id.* (Jackson, J., dissenting).

<sup>33</sup> See *id.* at 339–40 (Jackson, J., dissenting).

<sup>34</sup> *McLeod v. J. E. Dilworth Co.*, 322 U.S. 349, 353–54 (1944) (Rutledge, J., dissenting in *Dilworth* and concurring in *Gen. Trading Co.*).

<sup>35</sup> *Id.* at 350–51.



reasoned that both are “in fact and effect a tax levied on an interstate transaction.”<sup>36</sup> From the Due Process Clause perspective, both the “state of origin and [state] of market” have taxing power.<sup>37</sup> However, the dormant Commerce Clause requires more substantive consideration for the effect of the taxation.<sup>38</sup> The standard to be applied here is an analysis of the total burden of a given type of tax (i.e., the burden when all the states levy various types of taxes, and place cumulative, discriminatory, or special burdens on interstate commerce).<sup>39</sup> Justice Rutledge’s dissent in *Dilworth*, however, has another assumption as its rationale: All the state sales/use tax should be construed as a destination-based consumption tax.<sup>40</sup> Justice Rutledge defended the Arkansas tax in *Dilworth* as such a tax.<sup>41</sup> Justice Rutledge, like Justice Douglas, did not give the collection duty special consideration independent from substantive tax liability.

### C. *Miller Bros., Scripto, and Bellas Hess*

In *Miller Bros. Co. v. Maryland*, Justice Jackson’s opinion for the Court clarified several issues in construing the collection duty of an out-of-state retailer.<sup>42</sup> First, the question to be asked is whether imposing a duty to collect is within the reach of a state’s taxing power.<sup>43</sup> Second, the analysis of this legal concept has developed, not only from precedent regarding the Due Process Clause,<sup>44</sup> but also from the dormant Commerce Clause.<sup>45</sup> Third, there must be a link to justify the exercise of a state’s taxing power such as “domicile or residence,” “the situs of property,” “the keeping of tangible or intangible personalty,” “[c]ertain activities or transactions carried on within a state, such as the use and sale of property,” or “incorporation by a state or permission to do business there . . . .”<sup>46</sup>

In *Miller Bros.*, Maryland imposed a duty to collect use tax on a Delaware vendor on all goods it sold to Maryland residents and seized the vendor’s truck for failing to collect the tax.<sup>47</sup> The Court found that the original tax liability of Maryland residents did not provide grounds to impose a collection duty on an out-of-state

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<sup>36</sup> *Id.* at 357.

<sup>37</sup> *Id.* at 358.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* at 361.

<sup>41</sup> *See id.*

<sup>42</sup> *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344–46 (1954).

<sup>43</sup> *Id.* at 342.

<sup>44</sup> *Id.* at 344–45.

<sup>45</sup> *Id.* at 344.

<sup>46</sup> *Id.* at 345 (footnotes omitted).

<sup>47</sup> *Id.* at 341.

vendor.<sup>48</sup> The Court also distinguished the *Miller Bros.* case from *General Trading Co.*<sup>49</sup> In his dissenting opinion, Justice Douglas asserted that the majority's opinion would distort economic activity given that the state imposed only a minimal burden on the collector while there was sufficient contact between the vendor and the state.<sup>50</sup>

In *Scripto Inc. v. Carson*, Justice Clark's opinion for the Court identified the nexus between the state and the object of taxation by following the definite link or minimum connection standard of *Miller Bros.*<sup>51</sup> However, Justice Clark declared that the case was controlled by the holding in *General Trading Co.*<sup>52</sup>

It was *National Bellas Hess, Inc. v. Illinois* that formulated the physical presence rule, a standard mainly dependent on a vendor or seller's physical presence in a state.<sup>53</sup> The opinion of the Court, written by Justice Stewart, inferred from the preceding cases "[a] sharp distinction . . . between mail order sellers with retail outlets, solicitors, or property within a State, and those who do no more than communicate with customers in the State by mail or common carrier as part of a general interstate business."<sup>54</sup> In *Bellas Hess*, "[a]ll of the contacts which [Bellas Hess] . . . [had] with the State [were] via the United States mail or common carrier."<sup>55</sup> The Court sided with the putative obligor's constitutional objections to the collection and revoked the payment duty of use tax required by the Illinois statutes. Justice Fortas's dissenting opinion applied a less formalistic standard from the same cases and found in the facts of *Bellas Hess* "a sufficient nexus" to impose collection duty.<sup>56</sup>

#### D. *Complete Auto* and *Quill*

Until the advent of *Quill Corp. v. North Dakota*,<sup>57</sup> the cases on the collection duty of use tax were principally independent from those on state tax liability in general, although Justice Jackson suggested in *General Trading Co.* and *Miller Bros.* that

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<sup>48</sup> *Id.* at 347.

<sup>49</sup> *Id.* at 346–47.

<sup>50</sup> *Id.* at 357–58 (Douglas, J., dissenting).

<sup>51</sup> *Scripto, Inc. v. Carson*, 362 U.S. 207, 210–11 (1960).

<sup>52</sup> *Id.* at 210.

<sup>53</sup> *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill.*, 386 U.S. 753, 758 (1967).

<sup>54</sup> *Id.*

<sup>55</sup> *Id.* at 754.

<sup>56</sup> *Id.* at 761–62 (Fortas, J., dissenting) (internal quotations omitted).

<sup>57</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

the collection duty and tax liability are identical for the purpose of the Due Process Clause and the dormant Commerce Clause.<sup>58</sup>

In *Complete Auto Transit, Inc. v. Brady*, a Michigan motor carrier insisted that the Mississippi sales tax conflicted with the dormant Commerce Clause.<sup>59</sup> The tax was equal to five percent of the gross income of a transportation business in Mississippi.<sup>60</sup> The motor carrier claimed that the tax imposed a burden on the privilege of engaging in business in the state, and that its activity being interstate commerce, violated the holding in *Spector*.<sup>61</sup> The Court, however, simply overruled *Spector* in favor of the following four-pronged test:<sup>62</sup>

These decisions have considered not the formal language of the tax statute but rather its practical effect, and have sustained a tax against Commerce Clause challenge when the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the service provided by the State.<sup>63</sup>

This test undoubtedly rationalized the approach to constitutionalize a state tax under the dormant Commerce Clause. In fact, according to experts of constitutional law, the Court has since then “consistently followed” this test.<sup>64</sup> One of the remaining questions is how *Bellas Hess* would be analyzed under this test given that *Bellas Hess* did not precisely distinguish the Due Process Clause and the dormant Commerce Clause. Moreover, *Bellas Hess* was concerned not with tax liability itself, but with the collection duty.<sup>65</sup>

In *Quill*, the Court revisited the same question as *Bellas Hess*—whether a state may impose a duty to collect use tax upon a retailer that does not have a physical presence in the state.<sup>66</sup> The Court’s opinion, delivered by Justice Stevens, first declared that “[t]he two constitutional requirements,” the Due Process Clause on the one hand and the dormant Commerce Clause on the other, “differ fundamentally.”<sup>67</sup> For the first time, the Court

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<sup>58</sup> See *Gen. Trading Co. v. State Tax Comm’n of Iowa*, 322 U.S. 335, 339–40 (1944) (Jackson, J., dissenting); *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344 (1954).

<sup>59</sup> *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 274–76 (1977).

<sup>60</sup> *Id.* at 275.

<sup>61</sup> *Id.* at 278.

<sup>62</sup> *Id.* at 287–89.

<sup>63</sup> *Id.* at 279 (footnote omitted); see also *id.* at 277–78, 287 (rationalizing the four-pronged test).

<sup>64</sup> ERWIN CHERMERINSKY, *CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES* 480 (5th ed., 2015); see also *Quill Corp. v. North Dakota*, 504 U.S. 298, 310 (1992).

<sup>65</sup> *Nat’l Bellas Hess, Inc. v. Dep’t of Revenue of Ill.*, 386 U.S. 753, 758 (1967).

<sup>66</sup> *Quill*, 504 U.S. at 301–02.

<sup>67</sup> *Id.* at 305.

followed the distinction proposed by Justice Rutledge.<sup>68</sup> With regard to the Due Process Clause, by consulting the cases on judicial jurisdiction, the Court removed the element of physical presence in determining the link that justifies exercise of taxing power.<sup>69</sup> In other words, it overruled *Miller Bros., Scripto*, and *Bellas Hess* in this regard.<sup>70</sup> It concluded the collection duty in question did not conflict with the Due Process Clause.<sup>71</sup>

On the subject of the dormant Commerce Clause, *Quill* started from an analysis of the historical development of the cases.<sup>72</sup> Then, it took the facts of *Bellas Hess* through the four-pronged test of *Complete Auto* and concluded:

*Bellas Hess* concerns the first of these tests and stands for the proposition that a vendor whose only contacts with the taxing State are by mail or common carrier lacks the “substantial nexus” required by the Commerce Clause.<sup>73</sup>

The Court contended that *Bellas Hess* created a bright-line rule, or a safe harbor, in the first prong of the four-pronged test, which itself is a pragmatic standard.<sup>74</sup> Presumably it is difficult, if not impossible, to justify such a formalistic rule placed within a pragmatic standard from a policy standpoint. Therefore, Justice Stevens sought its foundation in “the doctrine and principles of *stare decisis* . . . .”<sup>75</sup>

In sum, through the general framework of the four-pronged test for state tax enunciated in *Complete Auto*,<sup>76</sup> *Quill* placed the case law on the collection duty in the first prong of *Complete Auto*.<sup>77</sup> However, whereas *Complete Auto* declined to follow the formalist approach of *Spector*<sup>78</sup> in favor of a more substantial one, *Quill* kept a formalistic element in the first prong.<sup>79</sup> Hence these decisions contain an implied conflict in their differing approaches.

#### E. The Significance of *Wayfair*

The Court’s opinion in *Wayfair*, written by Justice Kennedy, at last rejected the physical presence rule formulated by *Bellas*

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<sup>68</sup> *Id.* at 305–06 (citing *Int’l Harvester Co. v. Dep’t of Treasury*, 322 U.S. 340, 353 (1944) (Rutledge, J., concurring in part and dissenting in part)).

<sup>69</sup> *Id.* at 307–08.

<sup>70</sup> *Id.* at 306–08.

<sup>71</sup> *Id.* at 308.

<sup>72</sup> *Id.* at 306–08.

<sup>73</sup> *Id.* at 311.

<sup>74</sup> *Id.* at 314–15.

<sup>75</sup> *Id.* at 317.

<sup>76</sup> See *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

<sup>77</sup> *Quill*, 504 U.S. at 311–13.

<sup>78</sup> See generally *Spector Motor Serv., Inc. v. O’Connor*, 340 U.S. 602 (1951).

<sup>79</sup> *Quill*, 504 U.S. at 313.

*Hess* and *Quill* and overruled both cases.<sup>80</sup> The Court presented five reasons in rejecting the rule. The first three reasons concerned *Quill*.<sup>81</sup> First, the Court found that “the physical presence rule [was] not a necessary interpretation of” the first prong of the *Complete Auto* test.<sup>82</sup> It was “a poor proxy for the compliance costs faced by companies that do business in multiple States.”<sup>83</sup> Second, the Court noted that the rule distorted competition and worked as a tax shelter.<sup>84</sup> It disadvantaged local businesses and interstate businesses with a physical presence in the state.<sup>85</sup> Third, the rule was at odds with the case-by-case approach of the Court’s dormant Commerce Clause jurisprudence.<sup>86</sup> In addition, the Court pointed out that the application of the physical presence rule would be all the more inappropriate, given the advance of information technology in recent years.<sup>87</sup> Lastly, the Court claimed that the rule created unfair and unjust consequences for all concerned actors.<sup>88</sup>

As previously mentioned, the extent of the taxing power of a state is demarcated by two considerations: One is the limit of tax jurisdiction itself, and the other is the effects of the exercise of the taxing power.<sup>89</sup> The issue in *Wayfair* was the former. If, as Justice Rutledge had argued, the Due Process Clause exclusively dealt with the question of tax jurisdiction and, in contrast, the dormant Commerce Clause only with the question of the effects of the tax, *Quill* and *Wayfair* would not have been dormant Commerce Clause cases. In reality, *Complete Auto* kept the issue of jurisdiction within the ambit of the dormant Commerce Clause.<sup>90</sup> Accordingly, *Quill* and *Wayfair* dealt with the collection duty under the dormant Commerce Clause.<sup>91</sup> Nevertheless, assuming that the issue should be dealt with under the dormant Commerce Clause, *Wayfair* correctly ruled by opting for a case-by-case analysis instead of a bright-line physical presence rule.<sup>92</sup> However, *Wayfair* did not pay any attention to the fact that the tax liability in question was the collection duty of use

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<sup>80</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2099 (2018).

<sup>81</sup> *See id.* at 2092.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.* at 2093.

<sup>84</sup> *Id.* at 2094.

<sup>85</sup> *Id.* at 2094–95.

<sup>86</sup> *Id.*

<sup>87</sup> *Id.* at 2095.

<sup>88</sup> *Id.* at 2095–96.

<sup>89</sup> *See supra* Part I.A.

<sup>90</sup> *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 288 (1977).

<sup>91</sup> *Wayfair*, 138 S. Ct. at 2087; *Quill Corp. v. North Dakota*, 504 U.S. 298, 301 (1992).

<sup>92</sup> *See Wayfair*, 138 S. Ct. at 2094.

tax and that the economic burden of the tax itself was borne by consumers in the state.<sup>93</sup>

The Supreme Court's jurisprudence on collection duty of state consumption tax at this moment might be summarized as follows: The dormant Commerce Clause has strictly limited state's taxing power from both substantive and procedural aspects. In recent years, the substantive aspect has rarely been disputed in the context of state consumption taxes. But the second, third, and fourth prongs of the *Complete Auto* test will be applied to the cases on taxes.<sup>94</sup> Procedurally, an exercise of taxing power out of the jurisdiction is prohibited. The first prong of the *Complete Auto* test exactly examines this aspect.<sup>95</sup> *Wayfair* fine-tuned this examination by weighing physical elements to a lesser extent.<sup>96</sup>

## II. TAX COMPETITION AMONG LOCAL GOVERNMENTS IN JAPAN

### A. Outline of the Tax System in Japan

#### 1. Local Governments in Japan

Before referring to the tax system of Japan, this Article explains the basic structures of Japanese local governments. Japan is not a federal state—sovereignty is exclusively reserved for the national government. Japan's Constitution simply requires that a local system be constituted under the principle of local autonomy.<sup>97</sup> It says little about organization of local governments.<sup>98</sup> The Local Autonomy Act of 1947<sup>99</sup> adopts a two-tiered local government structure: forty-seven prefectures and approximately 1700 municipalities.<sup>100</sup> The municipalities cover all of Japan's territories.<sup>101</sup> This structure means Japan does not have unincorporated areas.<sup>102</sup> Even though prefectures do not have authority to control municipalities, all the municipalities belong to one of the prefectures.<sup>103</sup> In other words, every person living in Japan belongs to one of the municipalities and one of the prefectures. With regard to the function performed by the

<sup>93</sup> *See id.* at 2088.

<sup>94</sup> *Complete Auto Transit*, 430 U.S. at 278.

<sup>95</sup> *Id.*

<sup>96</sup> *Wayfair*, 138 S. Ct. at 2093 (“Physical presence is not necessary to create a substantial nexus.”).

<sup>97</sup> NIHONKOKU KENPŌ [KENPŌ] [CONSTITUTION], art. 92.

<sup>98</sup> *Id.* at art. 93.

<sup>99</sup> Chihō jichi hō [Local Autonomy Act], Law No. 67 of 1947.

<sup>100</sup> ATSURO SASAKI, MINISTRY OF INTERNAL AFFAIRS & COMM'NS, JAPAN, LOCAL SELF-GOVERNMENT IN JAPAN 3 (2014).

<sup>101</sup> *See id.* at 5.

<sup>102</sup> KURT STEINER, LOCAL GOVERNMENT IN JAPAN 169 (1965).

<sup>103</sup> Chihō jichi hō [Local Autonomy Act], Law No. 67 of 1947, art. 5, para. 2.



governments, municipalities are far more important than prefectures. Municipalities (or basic local governments as they are sometimes called)<sup>104</sup> play a major role in the everyday lives of its citizens.<sup>105</sup> Under Articles 2(2) and 2(3) of the Local Autonomy Act of 1947, the national government delegates to municipalities the power to regulate “local affairs” [chiiki ni okeru jimū] and other specifically enumerated affairs.<sup>106</sup> The role of prefectures in administering local affairs is subsidiary. Article 2(5) of the Act covers regional affairs, coordination of municipalities, and other affairs not appropriate for municipalities to administer.<sup>107</sup> Even from these affairs, some are designated for delegation to midsized or large municipalities located in the prefecture.<sup>108</sup>

Then, after World War II, the Supreme Commander for the Allied Powers (“SCAP”) required delegation of a wide variety of regulatory power to local governments.<sup>109</sup> As a result of major reforms of local governance during the past quarter century, municipalities acquired more power than before.<sup>110</sup>

## 2. Local Taxation in Japan<sup>111</sup>

The Constitution of Japan expresses nothing about the country’s tax system. It just declares that the payment of taxes is a duty of Japanese citizens<sup>112</sup> and requires the Diet to implement tax laws.<sup>113</sup> The substance of the tax system is entirely left to the Diet. With its broad authority, it chose a tax system that includes personal income tax, corporate income tax, inheritance tax, and value-added tax (“VAT”) as the source of revenue for the national government.<sup>114</sup> The VAT system is a European-type value-added

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<sup>104</sup> *Id.* at art. 2, para. 3.

<sup>105</sup> TOKYO METROPOLITAN GOVERNMENT, *The Structure of the Metropolitan Government*, <http://www.metro.tokyo.jp/ENGLISH/ABOUT/STRUCTSTR/structure01.htm> [<http://perma.cc/Z6BQ-HA9Z>].

<sup>106</sup> *Id.* at art. 2, paras. 2–3. The power to regulate “affairs” in Japanese local government law is identical to the “police power” in the U.S. law. See KURT STEINER, *supra* note 102, at 127–28.

<sup>107</sup> See Chihō jichi hō [Local Autonomy Act], Law No. 67 of 1947, art. 2, para. 5.

<sup>108</sup> Chihō jichi hō [Local Autonomy Act], Law No. 69 of 1946, art. 2, para. 4.

<sup>109</sup> See Terry MacDougall, *Towards Political Inclusiveness: The Changing Role of Local Government in Japan*, WORLD BANK INST. 1, 8 (2001), <http://documents.worldbank.org/curated/en/268371468260928014/pdf/330440wbi37169.pdf> [<http://perma.cc/X47M-BH3R>].

<sup>110</sup> See HIROSHI IKAWA, NAT’L GRADUATE INST. FOR POLICY STUDIES, 15 YEARS OF DECENTRALIZATION REFORM IN JAPAN 8–9, 12–26, 28 (2008), [www.jlgc.org.uk/en/pdfs/up-to-date\\_en4.pdf](http://www.jlgc.org.uk/en/pdfs/up-to-date_en4.pdf) [<http://perma.cc/S9PP-4N54>].

<sup>111</sup> For additional information on the tax system in Japan, see generally HIROMITSU ISHI, *THE JAPANESE TAX SYSTEM* (3d. ed. 2001).

<sup>112</sup> NIHONKOKU KENPŌ KENPŌ [KENPŌ] [CONSTITUTION], art. 30.

<sup>113</sup> *Id.* at art. 84. For the reader’s reference, the Diet is the national legislature of Japan.

<sup>114</sup> For background and additional commentary on the Japanese tax system, see Tadao Okamura, *The Japanese Tax System: Due Process and the Taxpayer*, 11 BERKELEY J. INT’L L. 125 (1993).

tax system, in which not only retailers, but also wholesalers cooperate in collecting the tax—unlike the American style sales tax, in which taxes are collected only by retailers.<sup>115</sup> Some portion of the tax revenue from VAT is automatically sent to local governments.<sup>116</sup> Local governments have personal income tax, corporate business/income taxes, and property tax as their own sources of revenue.<sup>117</sup> Local personal income tax and local corporate income tax make use of the tax base of national counterparts.<sup>118</sup> Although they are not technically a surtax to the national income taxes, they are essentially constituents of national income taxes. Property tax is the only tax that is reserved for local governments.

Up to this point, it appears that the tax jurisdiction is properly distributed among national and local governments. However, when the two levels of local governments—prefectures and municipalities—are taken into account, the tax revenue for the prefectures in rural areas tends to be insufficient as compared to urban areas. First, the local corporate income tax, which is the only major tax reserved exclusively for the prefectures, is highly volatile.<sup>119</sup> In addition, in part because the tax is allocated according to the number of offices and employees, the revenue from the taxes is concentrated in the metropolitan prefectures, especially Tokyo prefecture.<sup>120</sup>

As explained in the previous section, local governments play a crucial role in administrating local and other affairs. However, the local tax revenue is far less than the necessary amount to make ends meet. To make up for the deficit, the national government allots “tax” to the local governments. In order to mitigate interference with the decision-making of the local governments, the total amount of the allotted tax is statutorily determined.<sup>121</sup> The amount of allotted tax for a local government is calculated as follows: First, a standardized amount of expenditure is estimated from the population, the area, and other objective data of the local government.<sup>122</sup> Next, a standardized amount of tax

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<sup>115</sup> *Id.*

<sup>116</sup> Chihō zei hō [Local Tax Act], Law No. 226 of 1950, art. 72-114; *id.* at art. 72-115.

<sup>117</sup> *Id.* at art. 4, para. 2 (prefectures); *id.* at art. 5, para. 2 (municipalities).

<sup>118</sup> *Id.* at art. 32 (prefectural personal income tax); *id.* at art. 23, para. 1, no. 3 (prefectural corporate tax income); *id.* at art. 313 (municipal personal income tax); *id.* at art. 292, para. 1, no. 3 (municipal corporate income tax).

<sup>119</sup> See, e.g., EIJI TAJIKA & YUJI YUI, *Fiscal Decentralization in Japan: Does it Harden the Budgets of Local Governments?* in TACKLING JAPAN'S FISCAL CHALLENGES: STRATEGIES TO COPE WITH HIGH PUBLIC DEBT AND POPULATION AGING, INTERNATIONAL MONETARY FUND 126 (Keimi Kaizuka & Anne O. Krueger eds., 2006).

<sup>120</sup> See *infra* note 129, at 28–30.

<sup>121</sup> Chihō kōfuzei hō [Local Allocation Tax Act], Law No. 211 of 1950, art. 6.

<sup>122</sup> See *id.* at art. 10.

revenue is estimated by taking three quarters of the estimated tax revenue of the local government. The amount of allocation tax will be the balance of the standardized amount expenditure and the standardized amount of revenue.<sup>123</sup> A 25% percent discount gives local governments an incentive to increase their tax revenue as long as the estimated tax revenue does not exceed about 133% of the standardized amount of expenditure.<sup>124</sup>

### 3. Demarcation of Taxing Powers among Local Governments

There is no constitutional doctrine that delineates tax jurisdictions of local governments in Japan. This is natural because Japan's Constitution empowers the Diet to design the local government system. The national government delegates its taxing power to local governments as articulated by the Local Tax Act of 1950.<sup>125</sup>

Some insist that the Constitution guarantees local governments their own original power to tax. Surprisingly, a lower court decision in 1980 upheld the claim, although in dictum, by stating "such a statute that totally or virtually denies the taxing power of local governments is unconstitutional and void."<sup>126</sup> However, such a claim is ridiculous, to say the least. In the context of local governance, it is one thing to have a local government, but quite another that the government finances its resources only through its own tax revenue. Many countries, including Japan, transfer revenue between national/federal and local governments.<sup>127</sup> And as the decision itself makes clear, the claim does not put forward a meaningful standard to decide whether a given level of fiscal independence of a local government is sufficient to make it constitutional.

The Local Tax Act of 1950 does not contain any general provisions to limit local governments' exercise of taxing power. Despite that, we rarely find disputes concerning tax competition among local governments.<sup>128</sup>

The main reason is that the Act meticulously articulates the tax base, tax rate, and other features of principal taxes. The local governments have little room for exercising their power to tax

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<sup>123</sup> Chihō kōfuzei hō [Local Allocation Tax Act], Law No. 211 of 1950, art. 10.

<sup>124</sup> *See id.*

<sup>125</sup> *See* Chihō zei hō [Local Tax Act], Law No. 226 of 1950, art. 2.

<sup>126</sup> Fukuoka Chihō Saibansho [Fukuoka Dist. Ct.] June 5, 1980, Omuta-shi [City of Omuta, Fukuoka] v. Kuni [The Government of Japan], 417 HANREI TAIMUZU [HANTA] 51, 60.

<sup>127</sup> *See, e.g.*, Hansjörg Blöchliger & Claire Charbit, *Fiscal Equalisation*, 2008 OECD J.: ECON. STUD., 265, 277 (2008).

<sup>128</sup> For additional information on the tax scheme of Japan, see generally KENICHIRO HARADA, COUNCIL OF LOCAL AUTHS. FOR INT'L RELATIONS, LOCAL TAXATION IN JAPAN (2009).

freely. However, the Act does give local governments three kinds of flexibility.<sup>129</sup> First, the Act authorizes local governments to adopt higher tax rates that are different from the standard rate for any of the taxes.<sup>130</sup> Most of the prefectures use this “additional tax rate” [choka kazei] for prefectural per capita personal taxation, prefectural corporate per capita taxation, and prefectural corporate income taxation. Eight prefectures even use it for prefectural corporate business taxation. Some of the municipalities employ the additional tax rate for municipal corporate per capita taxation and municipal corporate income taxation. As of 2017, 153 out of 1719 municipalities apply additional tax rate on their local property tax. Whereas the standard rate for local property tax is 1.4 %, 141 municipalities apply a higher rate of 1.5%.<sup>131</sup>

Second, the Act authorizes municipalities to reduce or increase tax liability for several enumerated properties. For example, municipalities may impose tax against power plants for renewable energy at a lower rate or a higher rate.<sup>132</sup>

Third, the Act gives local governments power to introduce “extra-statutory” taxes. The legal issues regarding this concept will be discussed below. For now, it is sufficient to understand that the tax revenue from these taxes is relatively limited.<sup>133</sup>

## B. Extra-Statutory Taxation on Nuclear Plants

### 1. Introduction

Extra-statutory taxes are local taxes that a local government imposes without direct delegation from national legislation. They consist of two types of taxes. One is called an extra-statutory normal tax.<sup>134</sup> The other is an extra-statutory earmarked tax, which was newly introduced in 2000.<sup>135</sup> Most of the tax revenue of extra-statutory normal taxes is from taxes on nuclear fuel or other nuclear power related property.<sup>136</sup> Most of the tax revenue

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<sup>129</sup> Sōmushō jichi zeimu kyoku [MINISTRY OF INTERNAL AFFAIRS AND COMM'NS, LOCAL PUB. FIN. BUREAU], Chihou zeisei kankei shiryō [MATERIALS ON LOCAL TAX SYSTEM] 34 (2018).

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* at 56.

<sup>132</sup> *Id.*

<sup>133</sup> *Id.*

<sup>134</sup> Chihō zei hō [Local Tax Act], Law No. 226 of 1950, art. 4, para. 2, art. 5, para. 3 (prefectures and municipalities).

<sup>135</sup> *Id.* at art. 4, para. 6, art. 5, para. 7 (prefectures and municipalities).

<sup>136</sup> HARADA, *supra* note 128, at 26. In the 2016 fiscal year, tax revenue from taxes related to nuclear plants were 39.3 billion yen out of the total tax revenue of 51.7 billion yen from extra-statutory normal taxes. MATERIALS ON LOCAL TAX SYSTEM, *supra* note 131, at 37.

of extra-statutory earmarked taxes is from taxes on industrial wastes.<sup>137</sup> This section uses taxes on nuclear fuel as an example in demonstrating certain defects of the Japanese local tax system.

The origin of extra-statutory taxes lies in the practices in place in the pre-World War II era. Under the Ruling on Local Tax of 1880<sup>138</sup> and the Act on Local Tax of 1926,<sup>139</sup> there were many kinds of taxes imposed by local governments. At that time, the national statutes allowed prefectures to impose original taxes [zasshu ze]. However, these taxes greatly hindered smooth commerce between localities. The Local Tax Act of 1940<sup>140</sup> conditioned municipalities' introduction of an independent tax [dokuritsu ze] other than those enumerated in the Act, on the permission of the Minister of Internal Affairs<sup>141</sup> and the Minister of Finance. The Act abolished the original taxes and prohibited prefectures from imposing unenumerated independent taxes. After World War II, revisions to the Act in 1946 granted prefectures authority to impose unenumerated independent taxes.<sup>142</sup> The present Act, the Local Tax Act of 1950, renamed them extra-statutory taxes and allowed all local governments to adopt one under the permission [kyoka] of the Minister of Home Affairs.<sup>143</sup> The Act stipulated five conditions for the permission: actual existence of the source of revenue in the jurisdiction; demand for revenue sufficient to justify the proposed tax; the tax base is not the same as national taxes or other local taxes and imposition of the tax does not excessively burden the residents; the taxation does not greatly impede the commerce between the local governments; and the taxation must be appropriate from the perspective of the national government's economic policy.<sup>144</sup>

In 2000, as a part of a major reform of the local government system, the Diet gave local governments more discretion in levying extra-statutory taxes.<sup>145</sup> The revision of the Act in 2000

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<sup>137</sup> HARADA, *supra* note 128, at 26. In the 2016 fiscal year, tax revenue from taxes related to industrial wastes were 6.6 billion yen out of the total tax revenue of 10.1 billion yen from extra-statutory earmarked taxes. MATERIALS ON LOCAL TAX SYSTEM, *supra* note 131, at 37.

<sup>138</sup> Chihō ze kisosu [Rulings on Local Tax], Decree of the Cabinet No. 16 of 1880.

<sup>139</sup> Chihō ze ni kansuru hōritsu [Act on Local Tax], Law No. 24 of 1926.

<sup>140</sup> Chihō ze hō [Local Tax Act], Law No. 60 of 1940.

<sup>141</sup> The Ministry of Internal Affairs was later reorganized as the Ministry of Home Affairs and then the Ministry of Internal Affairs and Communications. See NOBUKI MOCHIDA, FISCAL DECENTRALIZATION AND LOCAL PUBLIC FINANCE IN JAPAN 10 (2008).

<sup>142</sup> The Local Tax Act of 1948 also authorized local governments to impose unenumerated independent taxes. See Chihō ze hō [Local Tax Act], Law No. 110 of 1948, art. 46, para. 2, and art. 103, paras. 2 and 3.

<sup>143</sup> See generally Chihō ze hō [Local Tax Act], Law No. 226 of 1950.

<sup>144</sup> *Id.*

<sup>145</sup> See HARADA, *supra* note 128, at 25.

replaced the permission by the Minister with his “consent” [dōi] to the proposal of a new tax.<sup>146</sup> And the Act required the Minister to consent to the proposal when the statutory conditions are met. The Act also dropped the first two conditions in the previous statute.<sup>147</sup> The 2004 revision of the Act imposed upon the local government a duty to ask for opinions of the taxpayers in proposing a new extra-statutory tax when the number of potential taxpayers is small and therefore only these taxpayers are supposed to bear heavy burden of the tax.<sup>148</sup>

## 2. The Advent of the Nuclear Fuel Taxes

The first local government that introduced nuclear fuel tax was the Fukui prefecture. The prefecture has had several nuclear reactors in the territory since 1970.<sup>149</sup> In the new year’s greeting of 1972, Heidayū Nakagawa, then the Governor of the prefecture, revealed his plan to launch a new extra-statutory tax on nuclear power plants.<sup>150</sup> His proposal was to reduce the profits of power companies and to transfer the amount reduced to the prefecture in which power plants were located.<sup>151</sup> Soon thereafter, then Prime Minister, Kakuei Tanaka, submitted an idea of new national tax on power plants. His idea became a tax for promotion of power-resources development.<sup>152</sup> The tax encourages local governments to accept power plants, including nuclear power plants.<sup>153</sup> The tax base of this tax is wholesale electric energy. The tax revenue from the tax is allocated to local governments as a subsidy.<sup>154</sup> However, like any other subsidy, the allocated funds are earmarked for limited power plant-related purposes. In light of such inconveniences inherent in the national tax and the accompanying subsidy, some local governments still wished for tax revenue from

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<sup>146</sup> See *id.*

<sup>147</sup> See *id.*

<sup>148</sup> Chihō zeī hō [Local Tax Act], Law No. 226 of 1950, art. 259, para. 2; art. 669, para. 2; art. 731, para. 3.

<sup>149</sup> For background information of the reactors, see J. Mark Ramseyer, *Nuclear Reactors in Japan: Who Asks for Them, What Do They Do?* (Harvard Law Sch. John M. Olin Ctr. for Law, Econ., and Bus., Discussion Paper No. 909, 2017), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2986410](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2986410).

<sup>150</sup> Hatsuden zeī shinsetsu wo junbi [*Preparing for Electricity Tax*], YOMIURI-SHIMBUN, Jan. 5, 1972, at 2.

<sup>151</sup> *Id.*

<sup>152</sup> Dengen kaihatu sokushin zeī hō [Act on Tax for Promotion of Power-Resources Development], Law No. 79 of 1974.

<sup>153</sup> Needless to say, the tax is one of the incentives the Japanese national government offers to local governments. For the analysis of these incentives, see J. Mark Ramseyer, *Why Power Companies Build Nuclear Reactors on Fault Lines: The Case of Japan*, 13 THEORETICAL INQUIRIES L. 457, 459, 479, 481 (2012), which points out that people rationally built nuclear power plants on fault lines.

<sup>154</sup> See Hiroshi Onitsuka, *Hooked on Nuclear Power: Japanese State-Local Relations and the Vicious Cycle of Nuclear Dependence*, 10 ASIA-PAC. J. 1, 7 (2012).



an extra-statutory tax. Because the tax base of an extra-statutory tax must not “be the same as existing national taxes or other local taxes,” taxing electric energy, which is already the object of the tax for promotion of power-resources development, does not seem to pass muster.<sup>155</sup> Nevertheless, in 1976, the Minister of Home Affairs permitted the proposal of nuclear fuel tax by Fukui prefecture.<sup>156</sup> The prefecture played a little trick here. It chose as the object of the tax the supply of nuclear fuel into the reactor.<sup>157</sup> The tax base is the price of the fuel. It thus avoided conflict with the statutory condition. It is unclear what sort of political negotiations occurred, however, it is reasonable to infer that the permission by the Minister originated not from mere interpretation of the Local Tax Act, but rather from some highly political considerations.

Having permitted the new tax of Fukui prefecture, the Minister was forced to permit other prefectures to impose identical or similar taxes: Fukushima (1977), Ibaraki (1978), Ehime (1979), Saga (1979), Shimane (1980), Shizuoka (1980), Kagoshima (1983), Miyagi (1983), Niigata (1984), Hokkaido (1988), Ishikawa (1992), and Aomori (2004) followed Fukui in imposing an extra-statutory tax on nuclear fuel.<sup>158</sup> All these taxes were valid for a limited time and have been subsequently renewed several times.<sup>159</sup>

### 3. The 2011 Fukushima Disaster and Its Effects on Nuclear Fuel Taxes

On March 11, 2011, a tsunami caused by a powerful earthquake hit the coasts of Iwate, Miyagi, and Fukushima prefectures.<sup>160</sup> Consequently, the nuclear reactors’ cores at the Fukushima Daiichi [Number One] power plant began to melt.<sup>161</sup> The power plant was closed, and the operations of all the other nuclear power plants were temporarily suspended. This essentially meant that the object of

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<sup>155</sup> See THE ASAHI SHIMBUN, Aug. 22, 1976, at 3.

<sup>156</sup> Fukui ken kakunenryo zei jorei [Ordinance on the Nuclear Fuel Tax of Fukui Prefecture], Ordinance (Fukui Prefecture) No. 40 of 1976.

<sup>157</sup> See Norihiko Kuwabara & Takufumi Yoshida, *Prefectures taxing nuclear plants until the bitter end*, THE ASAHI SHIMBUN (June 22, 2018), <http://www.asahi.com/ajw/articles/AJ201806220038.html> [<http://perma.cc/N3SU-CPXJ>].

<sup>158</sup> GREEN TAXATION AND ENVIRONMENTAL SUSTAINABILITY 219 (Larry Kreiser et al. eds., 2012).

<sup>159</sup> See *id.*

<sup>160</sup> Kenneth Pletcher & John P. Rafferty, *Japan Earthquake and Tsunami of 2011*, ENCYCLOPEDIA BRITANNICA (last updated Oct. 15, 2018), <https://www.britannica.com/event/Japan-earthquake-and-tsunami-of-2011> [<http://perma.cc/NUT9-47K2>].

<sup>161</sup> See *Fukushima Daiichi Accident*, WORLD NUCLEAR ASS’N (last updated Oct. 2018), <http://www.world-nuclear.org/information-library/safety-and-security/safety-of-plants/fukushima-accident.aspx> [<http://perma.cc/8JCT-E5WG>].

nuclear fuel taxes did not exist anymore. The prefectures suddenly lost all tax revenue.<sup>162</sup>

This incident changed the prefectures' policy on nuclear fuel taxes. As one consequence, Fukushima prefecture did not renew its ordinance on nuclear fuel tax and the ordinance lost its effect at the end of 2012.<sup>163</sup>

Further, other prefectures, having been dependent on the revenue from nuclear fuel taxes for a long time, sought means to collect money even when the reactors were shut down.<sup>164</sup> They revised the ordinances and began to impose a tax on the "business regarding operation and decommissioning of nuclear reactors."<sup>165</sup> Technically speaking, they modified the ordinances to make part of the tax base calculated on the thermal power [netsu shutsuryoku] of the reactors. Take Hokkaido (a prefecture) as an example, which has imposed this tax on Hokkaido Electric Power Company since September 2013.<sup>166</sup> The tax base is 5960 MW, the sum of the thermal power of the three reactors located in Tomari Power Plant, which is the only nuclear power plant in Hokkaido.<sup>167</sup> The tax rate is 37,750 yen per MW for three months.<sup>168</sup> Hence the annual tax revenue is 900 million yen.

Some prefectures began to impose other kinds of taxes on nuclear power plants. Three prefectures, Fukui, Ibaraki, and Aomori, levy taxes on power companies or reprocessing businesses for their imports and storage of spent nuclear fuel. The Aomori prefecture is the most conspicuous in this regard. The tax revenue from the tax on the handling of nuclear fuel materials [kakunenryo busshitsu to toriatukai ze] was a little less than 20 billion yen in 2016.<sup>169</sup> It reached nearly twenty percent of the 115 billion yen of

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<sup>162</sup> Kuwabara & Yoshida, *supra* note 157.

<sup>163</sup> Yuhei Sato, the Governor of Fukushima prefecture, emphasized that the tax policy is consistent with the prefecture's demand for nuclear decommissioning. *See Fukushima to Ax Nuclear Fuel Tax*, JAPAN TIMES (Nov. 21, 2012), <https://www.japantimes.co.jp/news/2012/11/21/national/fukushima-to-ax-nuclear-fuel-tax/#.W7GYgy-ZM6W> [<http://perma.cc/4REG-VP45>].

<sup>164</sup> Kuwabara & Yoshida, *supra* note 157.

<sup>165</sup> *See* Fukui ken kakunenryo ze jorei [Ordinance on the Nuclear Fuel Tax of Fukui Prefecture], Ordinance (Fukui Prefecture) No. 30 of 2016, art. 5, no. 2 (referring to both operation and decommissioning). *Cf.* Hokkaido kakunenryo ze jorei [Ordinance on the Nuclear Fuel Tax of Hokkaido], Ordinance (Hokkaido) No. 8 of 2013, art. 4 (referring only to operation of nuclear reactors).

<sup>166</sup> Kyodo, *Hokkaido Electric to Execute Second Price Hike*, JAPAN TIMES (Oct. 10, 2014), <https://www.japantimes.co.jp/news/2014/10/10/business/hokkaido-electric-execute-second-price-hike-november/#.XBsLfS2ZPOQ> [<http://perma.cc/FK3P-PE3A>].

<sup>167</sup> *See* HOKKAIDO ELECTRIC POWER CO., INC., <http://www.hepco.co.jp/energy/atomic/data/specification.html> [<http://perma.cc/L2K3-FK5Z>].

<sup>168</sup> *See* NUCLEAR FUEL TAX (last updated Aug. 28, 2018), <http://www.pref.hokkaido.lg.jp/sm/zim/tax/atom01.htm> [<http://perma.cc/5U8V-DKPQ>].

<sup>169</sup> *Id.*

the prefecture's tax revenue, excluding the amount of allocated consumption tax.<sup>170</sup>

#### 4. A Critical Appraisal of the Control on Extra-Statutory Taxes

##### a. The Nuclear Fuel Taxes and the Political Process

The nuclear fuel taxes are a mechanism used to incentivize local governments to accept nuclear power plants. Mark Ramseyer persuasively described the dynamics in which poor villages rationally, but shortsightedly, ask for subsidies at the cost of being the permanent location for nuclear power plants, which eventually render them unable to break from the resulting vicious cycle.<sup>171</sup> Admittedly, in analyzing nuclear fuel taxes thoroughly, the political process should be taken into consideration. Nevertheless, it is worth noting the defects of the Local Tax Act, particularly how its standards limit the taxing power of local governments. Even if certain transfers of wealth from a party to another should be considered desirable in the political process, it would not be achieved as the form of local tax had the national legislation strictly dismissed the alternative.

##### b. A Comparison with the Dormant Commerce Clause in the United States

This section identifies the problem with nuclear fuel taxes from the legal perspective. Next, this section examines which part of the Local Tax Act has given rise to such problems by comparing the statute with dormant Commerce Clause jurisprudence in the United States.

There are several problems with nuclear fuel taxes. The first is that their essential qualities are far from apparent. Particularly, it is not clear who the legislators intended to have bear the burden of the taxes. The power companies, or their shareholders, may be the tax bearers. Or it may also be the consumers of the electricity. However, because the taxes are considered to be the costs calculated in the electricity rates, it would be reasonable to assume that the consumers bear the tax burden.<sup>172</sup>

Second, since the consumers bear the tax burden, those who are subject to the taxes were never involved in determining the tax legislation. Nor do the consumers have any means to dispute

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<sup>170</sup> *Financial Situation*, AOMORI PREFECTURAL GOV'T. (last updated Nov. 2, 2018), [https://www.pref.aomori.lg.jp/soshiki/soumu/zeimu/files/H28\\_kenzei.pdf](https://www.pref.aomori.lg.jp/soshiki/soumu/zeimu/files/H28_kenzei.pdf) [http://perma.cc/3VAT-4BFX].

<sup>171</sup> Ramseyer, *supra* note 153.

<sup>172</sup> See Kuwabara & Yoshida, *supra* note 157.

the legality of the taxes against either the Local Tax Act or other national legislation.

Third, there is a problem with the recent modification of the taxes. All prefectures, other than Fukushima, revised their ordinances and began to impose taxes on the power companies, even when those companies do not operate nuclear reactors.<sup>173</sup> Because the reactors generate no electricity, such a tax cannot be a consumption tax (the economic burden of which would be borne by the consumers of electricity). However, neither the prefectures nor the Ministry of Internal Affairs and Communications give any reasoned explanation for this. In any case, it would be quite unreasonable to impose a fixed consumption tax irrespective of the level of consumption. The modification of the taxes has revealed that they are no more than simply a means to obtain a subsidy, as long as the nuclear power plants are located in their territories and there is no sensible justification for the taxes.

It is easy to see these problems stem from the absence of a Japanese equivalent to the dormant Commerce Clause. If Japan had a dormant Commerce Clause, it would have been possible to examine the validity of the nuclear fuel taxes using a test similar to the *Complete Auto* test.<sup>174</sup> For instance, the tax might be invalidated because it is not fairly related to the services the prefecture provides.<sup>175</sup> The tax on imports of spent nuclear fuel might conflict with the prohibition of discrimination against out-of-state actors.<sup>176</sup> In fact, as previously noted, the Local Tax Act needs only three requirements for the consent of the Minister of Internal Affairs and Communications.<sup>177</sup> These requirements do not allow for the invalidation of a tax that would harm the local tax system or domestic commerce.

Furthermore, there are at least two other serious defects in the Act. First, it is not clear when taxation against consumers outside the territory of the local governments is allowed, if at all. The Act provides that the source of income and location of the property must be within the territory before imposing taxes on income or property.<sup>178</sup> However, it does not spell out what principle governs the consumption taxes. Second, the Act says nothing about indirect taxes. The duty to ask for opinions of taxpayers, introduced by the revision of the Act in 2004, has

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<sup>173</sup> *See id.*

<sup>174</sup> *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

<sup>175</sup> *See id.*

<sup>176</sup> *See id.*

<sup>177</sup> *See HARADA, supra* note 128, at 25.

<sup>178</sup> Chihō zei hō [Local Tax Act], Law No. 226 of 1950, art. 262, 672, & 733-2.

nothing to do with the indirect taxes because the economic burden of them would be borne by people different from the taxpayers.

Let us go back to *Wayfair* now. In the cases on the collection duty of state use tax in the United States, the consumers within the state are the ones who bear the economic burden of the use tax.<sup>179</sup> The issue is whether the retailer that seems to have a scarce connection with the state is nevertheless obligated to collect tax from those consumers. In contrast, the nuclear fuel taxes in Japan are imposed on the power companies that have power plants in the territory of the local government. However, the tax burden is shifted to the consumers out of the territory. Both countries struggle in dealing with indirect consumption taxes. In the United States, by taking only the taxpayer into account, the fair apportionment of tax burden among the consumers in the state has failed, although *Wayfair* has mitigated the problem.<sup>180</sup> In Japan, by disregarding the consumers who bear the tax, the nuclear fuel taxes were implemented as an indirect vehicle for tax collection.

### C. The “Hometown Tax Donation” System

#### 1. Introduction

During the past decade, taxpayers’ attitudes towards Japanese local income taxation have drastically changed. The change was prompted by a newly-introduced tax credit regarding donations. Since the tax credit’s introduction in 2008, competition for donations among municipalities and prefectures has gradually accelerated through their offers of goods and services in return for donations.<sup>181</sup> This section will examine how the tax credit, and resulting behaviors of both local governments and taxpayers, can be seen as another example of how the local tax system in Japan is defective.

In Japan, local governments and the national government impose income taxes on their residents. Whereas there are many statutory provisions for the national income tax<sup>182</sup> and a large number of officials managing the national tax system, there are very few statutory provisions for local income taxes, with only a small number of officials hired to implement them. The reason for this is that local governments are largely dependent on the

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<sup>179</sup> See, e.g., *Quill Corp. v. North Dakota*, 504 U.S. 298, 302 (1992).

<sup>180</sup> See generally *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>181</sup> See Tomohiro Osaki, *Hometown ‘tax’ donations system catching on*, JAPAN TIMES (Oct. 20, 2014), <https://www.japantimes.co.jp/news/2014/10/20/reference/hometown-tax-donations-system-catching/#.W9jKBXpKiu4> [http://perma.cc/S5RT-CRFX].

<sup>182</sup> See *Shotoku zei hō* [Income Tax Act], Law No. 33 of 1965.

computation of income generated by the national income tax.<sup>183</sup> By referring to the tax base of the national income tax for the previous year, the local income taxes barely require their own computation process.

In spite of almost the same computation process, officials from the Ministry of Internal Affairs and Communications have forcefully insisted over time that the nature of the local income taxes is different from that of the national income tax.<sup>184</sup> They assert that the local income taxes represent the principle of fair share [*futan bun-nin*], one of the most important ideas in local taxation.<sup>185</sup> According to them, although this principle guides the entire local tax system, it is especially prominent for local income taxes because it justifies local governments' taxation against low-income people who are exempt from national income. The principle has also been referred to in justifying the fact that deductions and credits for various policy purposes are strictly limited in the local income taxes.

The local governments impose two kinds of "inhabitant taxes" [*jumin zei*] on individuals. One is per capita tax [*kinto wari*] on residents and nonresidents that have local establishments, such as land and buildings in the territory.<sup>186</sup> However, the amount and the significance of the per capita taxes is very small today. The other inhabitant tax is the local income taxes [*shotoku wari*] on the residents. These taxes are important in terms of their tax revenue.<sup>187</sup> They consist of the prefectural income tax and the municipal income tax.<sup>188</sup> The tax base for these taxes is almost the same as that for the national income tax. The standard tax rate<sup>189</sup> is four percent for the prefectural income tax<sup>190</sup> and six percent for the municipal income tax.<sup>191</sup>

<sup>183</sup> *Chihō zei hō* [Local Tax Act], Law No. 226 of 1950, art. 32 (prefectural personal income tax); *id.* at art. 23, para. 1, no. 3 (prefectural corporate income tax); *id.* at art. 313 (municipal personal income tax); *id.* at art. 292, para. 1, no. 3 (municipal corporate income tax).

<sup>184</sup> See generally Takeo Yamauchi, "*Kojin jumin zei no seikaku*" ni kansuru ichi kousatsu: "*futan bun-nin*" no imisuru mono (I) [A Consideration on the "Nature of Inhabitant Taxes": What "Fair Share" Means, Part I], 71 *JICHI KENKYU* 77, 80–85, 87–91 (1995) (showing an overview of the discourse on the principles of local taxation including the principle of "fair share").

<sup>185</sup> See TAX BUREAU, MINISTRY OF FIN., AN OUTLINE OF JAPANESE TAXES: 2001-2002, 16 (2002).

<sup>186</sup> The per capita taxes are also imposed on corporations and other entities that have establishments or dormitories in the territory of the local government. See Local Tax Act, Law No. 226 of 1950, art. 23, para. 1, no. 1; art. 24, para. 1, no. 1 & 2; art. 292, para. 1, no. 1; art. 294, para. 1, no. 1 & 2.

<sup>187</sup> See AN OUTLINE OF JAPANESE TAXES: 2001-2002, *supra* note 185, at 18.

<sup>188</sup> See *id.*

<sup>189</sup> The "standard tax rate" is the tax rate local governments apply under ordinary circumstances. However, the Act does not admit local governments to apply different rates for the local individual income taxes.



## 2. Transformation of the Local Income Taxes in the Past Decade

### a. An Introduction of Tax Credits for the Donation to Other Local Public Bodies

The 2008 revision to the Local Tax Act<sup>192</sup> drastically changed tax rules for donations, especially for donations to prefectures and municipalities other than the one in which the taxpayer's residence is located. The "hometown tax donation [furusato nozei]" system,<sup>193</sup> introduced by the revision, in essence expanded tax benefits for the taxpayers who made donations to local governments.<sup>194</sup> Before the revision, the amount of donation to local governments exceeding 5000 yen was deducted from income for the purpose of calculating the national income tax.<sup>195</sup> Deduction from the local income taxes was allowed only if the amount of donation exceeds 100,000 yen. The tax revision newly allowed a tax credit against local income tax liability for ten percent of the amount of donation if it exceeds 5000 yen. Given the fact that the aggregate tax rate of the local income taxes is ten percent, this tax credit means that the rate of local income taxes is zero for the amount of donations. Therefore, it is the same as a deduction of the amount of donations from taxable income. Furthermore, the revision offers another benefit to those who make donations to municipalities and prefectures. A new tax credit not exceeding one-tenth of the taxpayer's local income tax liability is granted for the amount of the donation.<sup>196</sup> Combined with the previously mentioned income deduction and tax credit, this "special" tax credit allowed a taxpayer who pays a fee of 5000 yen to transfer the amount equivalent to ten percent of his local income tax liability to whichever municipalities or prefectures he

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<sup>190</sup> Local Tax Act, Law No. 226 of 1950, art. 35, para. 1.

<sup>191</sup> *Id.* at art. 314-3, para. 1.

<sup>192</sup> Local Tax Act, Law No. 21 of 2008. See Tomoyuki Saisu, *Chihozeiho to no kaisei* [*The Revisions on the Local Tax Act*], Heisei 20 nen zeisei kaisei no kaisetsu [EXPLANATIONS ON THE 2008 TAX REVISION], 647-49 (2008).

<sup>193</sup> Technically speaking, the Japanese phrase "furusato nozei" connotes that the taxpayers "pay tax" to municipalities and prefectures and not that they "donate" money to these. However, we adopt here "hometown tax donation" as the translation of "furusato nozei" because it seems to be the official translation. See, e.g., *The Furusato Nozei Program: Tax Breaks with Benefits*, TOKYO WEEKENDER (Mar. 20, 2016), <https://www.tokyoweekender.com/2016/03/the-furusato-nozei-program-tax-breaks-with-benefits/> [http://perma.cc/UYW9-PW3R].

<sup>194</sup> For articles on the hometown tax donation system written in English, see Anthony Rausch, *A Paradox of Japanese Taxation: Analyzing the Furusato Nozei Tax System*, 15 ASIA-PAC. J. JAPAN FOCUS 1, 1 (2017) and Janet W. Kanzawa, *Lobsters, Hot Air Balloons, and the Hometown Tax: A Japanese Model for Revitalizing Rural Economies in the United States*, 2017 COLUM. BUS. L. REV. 1100, 1100 (2017).

<sup>195</sup> Income Tax Act, Law No. 33 of 1965, art. 78. The 2006 tax revision had reduced the minimum amount from 10,000 yen to 5000 yen. *Id.*

<sup>196</sup> Local Tax Act, Law No. 226 of 1950, art. 37-2, para. 2, and art. 314-7, para. 2.

or she chooses. In essence, by paying 5000 yen, a taxpayer obtains the right to make his donation to local governments a substitute for his tax payment.<sup>197</sup>

The report prepared by the committee of experts on local governance offers two justifications for the hometown tax donation system.<sup>198</sup> One is that a taxpayer should be allowed to pay tax to his own hometown municipality or prefecture from which he has benefited in his or her younger years. In other words, the donation is a deferred payment of consideration for past public services. The other is that the system acts as an incentive for municipalities and prefectures to compete to provide better public services, not only to their own residents, but also to other citizens as a whole. This explanation expects that the amount of donations a local government assembles would stand for the popularity of the policies it chooses. In other words, it hopes for a taxpayer—instead of a consumer-voter in the Tiebout model—to pick a local government which best satisfies his or her preference pattern for public goods.<sup>199</sup>

A disparity of tax revenue among municipalities and prefectures is in the background of the hometown tax donation system.<sup>200</sup> Local governments in the urban and industrial area such as the Tokyo prefecture and the city of Nagoya have a large amount of tax revenue from the local income tax, especially the local corporate income tax.<sup>201</sup> Conversely, those in rural areas have difficulty making ends meet and are heavily dependent upon “local allocation tax [chiho kofu ze]” from the central government.<sup>202</sup> Accordingly, amelioration of the imbalance was one of the main motives for the idea of hometown tax donation. However, it entirely fails to accomplish this purpose. There is no assurance that the taxpayers will act optimally in order to transfer the tax

<sup>197</sup> For a discussion of this system, see *Hometown tax donation system*, JAPAN TIMES (Mar. 11, 2017), <https://www.japantimes.co.jp/opinion/2017/03/11/editorials/review-of-the/#.XB159C2ZPOQ> [<http://perma.cc/2KJ9-XDH7>].

<sup>198</sup> For an analysis, see Hideaki Sato, “*Furusato nozei kenkyukai hokokusho*” to *Furusato nozei seido* [“*The Report of the Committee on Hometown Tax Donation*” and the *System of Hometown Tax Donation*], 1366 JURISUTO 157 (2008) (containing the explanations of a member of the committee for the report).

<sup>199</sup> See Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416, 417–18 (1956) (proposing a model in which a consumer in a given municipality, instead of voting to change the policy of the community, physically moves to another municipality for policy that best satisfies his preference for public goods).

<sup>200</sup> Takuji Koike, *Chiho zaisei kaikaku to zeishu no chiiki-kan kakusa* [The Reform of Local Public Finance and the Disparity of Tax Revenue Among Localities], 593 CHŌSA TO JOHŌ 1 (2007).

<sup>201</sup> See James Mayger & Hannah Dormido, *The Rich are Getting Richer in Abe’s Japan*, BLOOMBERG (Dec. 13, 2017), <https://www.bloomberg.com/graphics/2017-japan-inequality/>.

<sup>202</sup> See JURO TERANISHI, *EVOLUTION OF THE ECONOMIC SYSTEM IN JAPAN* 46, 207 (2005).

revenue from the rich local governments to the poor local governments at the appropriate level.

For the purpose of the calculation of local allocation tax, the amount of a donation is deducted from the tax revenue of the residence municipalities/prefectures, but is not added to the tax revenue of the receiving municipalities/prefectures.<sup>203</sup> The rule means that the reduction of tax revenue for a local government caused by the resident's donation to other local governments is considerably supplemented by an increase in the amount of local allocation tax.<sup>204</sup>

#### b. The Emergence of “Governmental” Tax Shelters through Rewards to the Donation

Even though many might have considered the idea of hometown tax donation attractive, only a small number of taxpayers dared to disburse 5000 yen to donate to other local governments. Most taxpayers' indifference was reasonable. They had no motive at all to make donations to local governments when they do not enjoy the benefit from the donation in a tangible form. It is worth noting that, after the earthquake and tsunami of 2011, some funds were sent through the system of hometown tax donation to the local governments that were affected.<sup>205</sup> This incident, however, did not accelerate the use of the system at a significant degree. As a result, the legislators then dropped the cost for the taxpayers from 5000 yen to 2000 yen in 2012.<sup>206</sup> However, the effect of this revision was also limited.

Then, several municipalities started to “reward” the donation, which gradually changed the state of affairs. Since 2012, with the help of web portals created by enterprises such as Trustbank (furusato choice), Rakuten (Rakuten furusato nozei), i-mobile (furunavi), Satofull, a subsidiary of Softbank (Satofull), JTB (furupo), All Nippon Airways (ANA no furusato nozei), etc., the amount of hometown tax donation saw an upsurge.<sup>207</sup>

The fair market value of the reward to the donation seems to be about half of the amount of donation on average, though it

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<sup>203</sup> Saisu, *supra* note 192, at 649.

<sup>204</sup> See Masakatsu Misumi, *Jiko futan naki “kifu” no arikata ga towareru “furusato nozei”* [*Hometown Tax Donation: A Questionable “Donation” without Real Burden*], 371 RIPPŌ TO CHŌSA 59, 70 (2015) (explaining in figure 14 the economic burden of actors with respect to hometown tax donation).

<sup>205</sup> See Osaki, *supra* note 181.

<sup>206</sup> See *Hometown tax donation system*, *supra* note 197.

<sup>207</sup> The names of the services they provide are indicated in the parentheses.

depends on the policy of each local government.<sup>208</sup> For example, according to the Satofull website, the market value of the reward given by Ureshino city in the Saga prefecture is almost fifty percent of the amount of donation: A bottle of sake brewed in the city under the brand of “Azumacho,” the market price of which is 5400 yen including VAT at eight percent, is on the list to choose from for those who have made 10,000 yen of donation.<sup>209</sup> Similarly, a set of six plates of porcelain and a dice made of porcelain manufactured in a pottery in the city, the market price of which is 10,800 yen including VAT, is on the list for those who have contributed 20,000 yen as hometown tax donation.<sup>210</sup>

The upsurge of the amount of donations in 2014 prompted those municipalities and prefectures that have been reluctant to introduce rewards for the hometown tax donation to join the competition for donation. If a local government restrained itself from offering rewards, it would continue to lose tax revenue from its residents’ donation to other local governments. The 2014 tax revision spurred the race by raising the maximum amount of the “special” tax credit from ten percent of his local income tax liability to twenty percent.<sup>211</sup> It also simplified the procedure for making the hometown tax donation by exempting most taxpayers from the duty of filing their tax returns, who previously had to file them only for the purpose of the donation.

As previously explained, the original intent of the hometown tax donation system was just to allow taxpayers to choose local governments to which they pay their local income taxes and, by doing so, to alleviate the disproportionate financing ability among the local governments to a certain degree. However, emergence of the practice of rewards and accompanying popularity of the system

<sup>208</sup> For an analysis of the state of affairs in 2018, see Taro Hagami, *Furusato nozei sontoku kanjo wasuto besuto 50* [Profit and Loss from the Hometown Tax Donation: The Top 50 and the Bottom 50 Municipalities], 1614 CHŪO KŌRON 154 (2018).

<sup>209</sup> *Saga ken Ureshino shi* [Ureshino City, Saga], *Junmai daiginjo homon azumacho 1.8L*, SATOFULL, [https://www.satofull.jp/products/detail.php?product\\_id=1000943](https://www.satofull.jp/products/detail.php?product_id=1000943) [<http://perma.cc/A4MM-Q4FB>] (offering a sake bottle of “Junmai daiginjo homon azumacho” as the reward for a 10,000 yen donation). Cf. *Homon azumacho junmai daiginjo 1.8L*, SAITO SHOTEN, <http://www.saito-sake.com/shopdetail/005002000001/> [<http://perma.cc/PS7L-XVR4>] (selling the same sake bottle at a liquor shop for 5400 yen via the internet).

<sup>210</sup> *Saga ken Ureshino shi* [Ureshino City, Saga], *Hizen yoshida yaki ji no sakazuki yojo han shuki setto*, SATOFULL, [https://www.satofull.jp/products/detail.php?product\\_id=1013293](https://www.satofull.jp/products/detail.php?product_id=1013293) [<http://perma.cc/CF6Y-6U8Y>] (offering a set of six plates of porcelain and a dice made of porcelain as the reward for a 20,000 yen donation). Cf. *Tsujiyō seitojo yojo han shuki*, JI NO SAKAZUKI, <https://jinusakazuki.thebase.in/items/3290714> [<http://perma.cc/AT5Q-J2GJ>] (selling the same porcelain and dice set at a local pottery shop for 10,800 yen via the internet).

<sup>211</sup> See Takuya Shimomura, *Chihozeiho to no kaisei* [The Revisions on The Local Tax Act], *Heisei 27 nen zeisei kaisei no kaisetsu* [Explanations on the 2015 Tax Revision], 932–36 (2015).

gave the system an unexpected role. It has turned into means to vitalize local economy. To reward donors, local governments now have to purchase their local goods and services from businesses in their territories. And it is natural for the legislators to reinforce this excellent method of subsidizing local governments that try hard to vitalize their local businesses.

### 3. A Critical Appraisal of the Policy

To evaluate the hometown donation system precisely, we have to know who the system benefits and who bears its costs. While credible data is not available, this section considers two possibilities.

At one extreme, the taxpayer who makes a donation might not change his or her consumption patterns at all. He or she may just reduce purchase of consumption goods and acquire them as the rewards for the donation. In this case, the tax donation system works as an offer of tax reduction. The system is nothing but a tax shelter benefiting the taxpayer.<sup>212</sup> In this setting, all the benefit from the system is absorbed by the taxpayer and the local government. The system will not be beneficial to local businesses to any extent because, as the sales of the goods to the local government increase through the reward to the donation, the sales to the consumers will decrease.

However, it is unrealistic to suppose the taxpayers will not change their consumption patterns at all. Presumably, the taxpayers will change the goods or services they consume. Therefore, at the other extreme, they might keep their previous consumption patterns and acquire additional goods and services through the donation tax system. To the extent they increase consumption, the system might be justified as a tool for stimulating the domestic economy.

Yet as far as the newly acquired goods and services through the hometown tax system replace the previously consumed goods and services, the system together with the rewards might distort the market economy. If the goods and services the taxpayers have formerly consumed have been produced in one municipality, then the system merely substitutes them with those produced in the other municipality at the expense of the national treasury. Obviously, encouraging such a zero-sum game is not a reasonable policy. If the goods and services have been imported from abroad, then the system is nothing more than subsidies to the domestic

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<sup>212</sup> An opportunity of investment for taxpayers the expected return of which is positive after tax, which is normally contrived and sold by financial institutions, is known as a "tax shelter." A donation to local public bodies under the hometown tax donation system is nothing but a tax shelter, even though the local governments instead of financial institutions offer the chance for it.

industries. In sum, the hometown tax donation system possibly harms the domestic and international commerce as a whole, even if it effectively energizes the economy in some local governments of Japan. It benefits local businesses at the sacrifice of the businesses out of the territory.

If Japan had a dormant Commerce Clause, the rewards for the donation would be invalidated because they unquestionably disturb the domestic commerce. The Clause would invalidate them because the burdens on the domestic commerce outweigh the overall benefits of the policy. In addition, although it might be difficult to argue that the rewards discriminate out-of-staters, they directly harm other local governments. In reality, none of the articles in the Local Tax Act effectively stop the rewards. The Ministry of Internal Affairs and Communications just asks local governments to act according to the principles of the hometown tax donation system.<sup>213</sup> Only a part of local governments obey the guidance.

#### CONCLUSION

As the nuclear fuel taxes and the hometown tax donation demonstrate, tax competition among local governments in Japan is accelerating. This harms market economy by making it less efficient and fails to redistribute wealth. The present circumstances in Japan remind us of the essential function of the dormant Commerce Clause. It plays an important role in implementing basic principles of fiscal federalism. Even though *Wayfair* did not fully scrutinize the nature of indirect tax and paid little attention to the character of collection duty as it differs from ordinary tax liability, this United States Supreme Court decision expanded the range of the application of the legal doctrine and should be respected.

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<sup>213</sup> See, e.g., MINISTER OF INTERNAL AFFAIRS AND COMMUNICATIONS, *Furusato nozei ni kakaru henreihin no sofu to ni tsuite* [ON THE REWARDS FOR HOMETOWN TAX DONATION] (2017); Sōmushō jichi zeimu kyoku [MINISTRY OF INTERNAL AFFAIRS AND COMM'NS, LOCAL PUB. FIN. BUREAU], *supra* note 131, at 130–32 (providing administrative guidance on the rewards for hometown tax donation).



# Government Imprudence and Judicial Decisions in Domicile Reservations: A Comparative Analysis between India and the United States

*Tania Sebastian\**

## INTRODUCTION

The labyrinth of anachronism relating to the concept of ownership of resources by the state that can be used by its own residents, the resulting burden on interstate commerce, accompanied by the rationale of reducing unemployment in the state, the impediments that affect the free flow of labor, and the constitutional defects in the state's role and its function in the local hiring plan, are all issues that courts have to remedy.

This Article compares the hiring practices and preferences of local residents in the United States of America (U.S.) with India. Such analysis is relevant as level playing field doctrines have been used indefinitely to justify specific reservations in employment. While reservations for backward communities come within the constitutional scheme of India, this Article probes into the acceptance and constitutionality of reservations in employment. Further, this Article looks into the constitutionality of vertical reservations and justifications given by states for these types of reservations. The continued litigation in this area, even with decisions of the Supreme Court of India striking down unjustifiable vertical reservations for domicile preferences, speaks volumes about governments' imprudence relating to notifications for resident-based hires and domicile preferences given to residents. The Supreme Court of India has also been riddled with the calculations and implementation of horizontal reservations. Various state high courts in India have shown indecisiveness in their judgments with contradictory positions. These observations are made in light of the U.S. Constitution's Commerce Clause and Privileges and Immunities Clause. In short, the United States' justifications

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and court decisions can be examined and contrasted with the Indian jurisprudence as a learning experience for both nations.

Both nations have set legislative boundaries stipulating what is and what is not acceptable as a hiring preference depending upon the use of local human resources and natural resources, which are then tested by the judiciary for validity. In examining the need to uphold local hiring principles, courts have tested these hiring preferences using constitutional and statutory principles. On the other hand, the main legislative aim is to reduce unemployment in the respective states.

This Article restricts its analysis to the Alaska Hire doctrine and looks at an aspect that deals more with employment rather than control over natural resources,<sup>1</sup> so that a comparison with India can be explored. This analytical restriction is necessary as the comparative system of India primarily focuses on employment under the analogous resident hire principle envisaged as an exception to Article 16 of the Constitution of India.<sup>2</sup> The limitation of this Article lies in the difference in the structure of governance of both nations, with the U.S. government functioning as a federal form of government and India as a combination of federal and unitary.<sup>3</sup> The difference in the division of powers results in states behaving differently and having varying rationales in judgments across the two jurisdictions. In spite of these differences, the regulation of interstate commerce and interstate movement in the two legal regimes are scrutinized in this Article.

## I. INDIA

### A. Affirmative Action and Vertical Reservation in the Indian Framework

Local hiring preferences cannot be discussed in a vacuum without the background of affirmative action. The history of discrimination and subjugation is sought to be remedied by affirmative action. Affirmative action is a remedy to past discrimination faced by minorities and is utilized to ensure that there is a better position to place them in this compassionate scheme of the Constitution of India.<sup>4</sup> It is designed to remedy the systematic unfairness that ran through centuries and

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1 See *Hicklin v. Orbeck*, 565 P.2d 159, 172–73 (Alaska 1977).

2 See INDIA CONST. art. 16.

3 See CONSTITUENT ASSEMBLY DEBATES, 11 THE CONSTITUENT ASSEMBLY OF INDIA 617–18 (Nov. 17, 1949) (stating that the Constitution of India does not present itself as federal or unitary, but a peculiar combination of both).

4 See M. Varn Chandola, *Affirmative Action in India and the United States: the Untouchable and Black Experience*, 3 IND. INT'L & COMP. L. REV. 101, 101–02 (1992).

generations.<sup>5</sup> These minorities were predominately based on gender, caste, and religion.

Courts in India (and the U.S.) have upheld the constitutional mandates of affirmative action,<sup>6</sup> with the simple logic of treating all citizens as equal,<sup>7</sup> while recognizing that unequals cannot be treated equally.<sup>8</sup> The Indian Constitution, in fact, expressly provides for affirmative action and “reservations,” or quotas.<sup>9</sup> These reservations are for backward classes of citizens, and include, as part of the constitutional scheme, Schedule Castes, Schedule Tribes, and Other Backward Castes.<sup>10</sup> These groups are bound together by the terminology of vertical reservation. Horizontal reservations are for categories of persons with disabilities, women, and ex-servicemen; vertical reservation encompasses domicile-based reservation.<sup>11</sup> Various cases discussed in the forthcoming parts of this Article have understood that horizontal reservation cuts across vertical reservation and that the most effective manner in which both vertical and horizontal reservations can co-exist is through inter-locking reservation.<sup>12</sup> Candidates selected against the quota for horizontal reservation will be placed within the vertical reservation in the appropriate category. This appropriate category depends upon their original category to which they belong in the roster meant for reservation of Schedule Castes, Schedule Tribes, and Other Backward Castes.

## B. The Beginning: Horizontal Reservations in India

Horizontal reservation is a reservation for women and persons with physical handicaps under Article 16 of the Constitution of India.<sup>13</sup> Article 16(1) of the Constitution of India states that in matters of public employment, “[t]here shall be equality of opportunity for all citizens.”<sup>14</sup> Article 16(3) mentions an exception to this rule:

Nothing in this article shall prevent Parliament from making any law prescribing, in regard to a class or classes of employment or appointment to an office under the Government of, or any local or

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<sup>5</sup> *See id.* at 101.

<sup>6</sup> *See, e.g.,* Akhil Bharatiya Soshit Karmachari Sangh v. Union of India, 1981 AIR 298 (India); State of Kerala v. N.M. Thomas, 1976 AIR 490 (India).

<sup>7</sup> *See* INDIA CONST. art. 14.

<sup>8</sup> *See* Chandola, *supra* note 4, at 107.

<sup>9</sup> *Id.* at 105–06.

<sup>10</sup> *See id.* at 106.

<sup>11</sup> *What is Vertical Reservation and Horizontal Reservation?*, GOVTSTAFFNEWS, <http://govtstaffnews.in/what-is-vertical-reservation-and-horizontal-reservation/> [<http://perma.cc/RD5L-7DLB>].

<sup>12</sup> *See* Indra Sawhney v. Union of India, AIR 1993 SC 477, para. 95 (India).

<sup>13</sup> INDIA CONST. art. 16.

<sup>14</sup> INDIA CONST. art. 16, § 1.

other authority within, a State or Union territory, any requirement as to residence within that State or Union territory prior to such employment or appointment.<sup>15</sup>

As one of the two types of reservation, horizontal reservation is named as such for simplifying the types of reservation and affirmative action envisaged under the Constitution of India.

The Indian judicial trend in deciding cases under Article 16(3) includes the Supreme Court and the High Court decisions of various states. For example, a Uttarakhand High Court decision in March 2018 dealt with a ten percent horizontal reservation as advertised by the government that was ultimately declared unconstitutional.<sup>16</sup> The government's stance and notification were scrutinized under Article 16.<sup>17</sup> The contention was that the Government Order (G.O.) dated August 11, 2004, provided persons who are domiciled in the State of Uttarakhand and are identified as "andolankaris" (those who had participated in the Uttarakhand movement and have sustained injury during that movement and remained in jail for seven days or more) with horizontal reservation.<sup>18</sup> However, the G.O. was never a Government Order. Instead, it was a Circular issued by the Principal Secretary, Government of Uttarakhand, that was not notified in the State Gazette, and had been held unconstitutional in an earlier case.<sup>19</sup>

Nevertheless, the Government of Uttarakhand issued Circulars from time to time for appointment of "andolankaris" for Group "C" and Group "D" posts<sup>20</sup>—an action that the court found arbitrary. Pointing out the government's imprudence, Justice Lokpal stated that such a provision that flows from the G.O. "does not come within the ambit of provisions of Article 16(4) of the Constitution of India" that speaks about "provision[s] for the reservation of appointments or posts in favour of any backward class of citizens which, in the opinion of the State, is not

<sup>15</sup> *Id.* at art. 16, § 3.

<sup>16</sup> *See* In the matter of appointments of activists on Group 'C' and Group 'D' posts under the Uttarakhand Rajya Andolan Ke Ghayal/Jail Gaye Andolankariyon Ki Sewayojan Niyamawali, 2010 v. State of Uttarakhand, WP No. 67 of 2011, paras. 22, 26 (Uttarakhand HC, Mar. 7, 2018) (India), <https://indiankanoon.org/doc/52637647/> [<http://perma.cc/3KZ6-VUCK>] (following a divided opinion on appeal by a division bench comprising of Justices Sudhanshu Dhulia and U.C. Dhyani this case was heard by a single bench).

<sup>17</sup> *See id.* at paras. 19–22.

<sup>18</sup> *See id.* at para. 4.

<sup>19</sup> *See id.* at para. 6. Later in the judgment, more clarity is provided on the fate of the Circulars: "It is worth mentioning here that the Circular Letter dated 11.08.2004 was quashed by learned Single Judge of this Court, vide judgment and order dated 11.05.2010, passed in Writ Petition no. 945 (S/S) of 2007 and connected writ petition, holding the said Government Order as violative of Article 14 and 16 of the Constitution of India." *Id.* at para. 26.

<sup>20</sup> *See id.* at paras. 4–5.

adequately represented in the services under the State.”<sup>21</sup> Further, the callous nature of the government in determining the type of reservation is also reflected in the fact that no data was collected before issuing the Circulars giving appointments to “andolankaris.”<sup>22</sup> Justice Lokpal also noted that the reservations were to be given without holding any competitive examination amongst them<sup>23</sup> which is in itself a clear violation of Articles 14 and 16(1) of the Constitution of India. Justice Lokpal goes on to state that “this is not even a reservation, but a form of gratuitous or compassionate appointment, which is clear violation of Article[s] 14 and 16 of the Constitution of India.”<sup>24</sup> And further that “the classification of ‘andolankaris’ is not based on any intelligible differentia which can distinguish ‘andolankaris’ from the many left out of the group and secondly the classification has no rational relation with the object sought to be achieved.”<sup>25</sup>

### C. The Analogous Concept of Resident Hire Principle in India: An Example

In December 2016, a controversial draft amendment to the Karnataka Industrial Employment (Standing Orders) Rules of 1961 was announced by the Government of Karnataka with the aim of providing a one hundred percent reservation for the local residents (known as “Kannadigas”) in private sector industries (except the Information Technology and Biotechnology sectors).<sup>26</sup> This amendment was to be applied across the state for certain categories of jobs that had obtained government concessions based on land, electricity, water, tax rebate, or deferment of tax as per Industrial Policy. A subsequent violation of the draft amendment would cancel these government concessions, hence compelling the private sector to implement the draft amendment. When announced to the public, a host of issues were discussed, most of all, the issue of loss of revenue by closing down options of hire from other states and its negative impact on labor mobility

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<sup>21</sup> *Id.* at paras. 20(4), 22.

<sup>22</sup> *Id.* at para. 23.

<sup>23</sup> *Id.* at paras. 6–7 (citing C.L. no. 1269 of 2004).

<sup>24</sup> *Id.* at para. 30.

<sup>25</sup> *Id.*

<sup>26</sup> See generally Karnataka Industrial Employment (Standing Orders) Rules (1961) (India) (demonstrating a lack of reservation for local residents in private sector industries); see also *Insights into Editorial: Karnataka’s Dangerous New Reservation Policy*, INSIGHTSIAS (Dec. 26, 2016) (showing that these private sectors have not been covered by the Karnataka Industrial Employment (Standing Orders) Rules of 1961 for a period of five years beginning in 2014, hence they were not affected by the draft amendment), <http://www.insightsonindia.com/2016/12/26/insights-editorial-karnatakas-dangerous-new-reservation-policy/> [<http://perma.cc/MT84-Y7NG>].

were brought to the forefront. In India, with mobility enshrined in the constitution, statistics show that inter-country mobility for job seekers is high.<sup>27</sup> This is in consonance with Article 19 of the Constitution of India that states that “all citizens shall have the right to move freely throughout the territory of India and to reside and settle in any part of the territory of India.”<sup>28</sup> Other than the fundamental right, Article 301 of the Constitution of India states that there shall be “[f]reedom of trade, commerce and intercourse [s]ubject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.”<sup>29</sup> Interestingly, this draft amendment was not pushed forward and the draft itself was made unavailable.<sup>30</sup>

#### D. The Resident Preference Dilemma Examined: Articles 15 and 16 of the Constitution of India

Article 15(2) of the Constitution of India bars discrimination on “grounds only of religion, race, caste or sex and place of birth . . . .”<sup>31</sup> The reasonableness under Article 15 is maintained by flexibility given to make special provisions for women and children, and to make “any special provision for the advancement of any socially and educationally backward classes of citizens or for the Scheduled Castes and the Scheduled Tribes,” should the state feel the need to do so.<sup>32</sup> Equality of opportunity in matter of public employment is found under Article 16 of the Constitution of India, which advocates a non-discriminatory policy. Article 16(2) provides that “no citizen shall, on grounds only of religion, race, caste, sex, descent, place of birth, residence or any of them, be ineligible for, or discriminated against in respect or, any employment or office under the State.”<sup>33</sup> Nevertheless, Article 16(3) states that:

Nothing in this article shall prevent Parliament from making any law prescribing, in regard to a class or classes of employment or appointment to an office under the Government of, or any local or other authority within, a State or Union territory, any requirement as

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<sup>27</sup> See LAVEESH BHANDARI & PAYAL MALIK, INDIA’S BORDERLESS WORKFORCE: A MANPOWER INDIA WHITE PAPER 8 (2018), <https://www.manpower.com/wps/wcm/connect/ec7b7b30-b9c3-4684-afc4-750fdb5e94a8/Indias+Borderless+Workforce.pdf?MOD=AJPERES> [<http://perma.cc/W2VL-KDGG>].

<sup>28</sup> INDIA CONST. art. 19.

<sup>29</sup> *Id.* at art. 301.

<sup>30</sup> See *Insights into Editorial: Karnataka’s Dangerous New Reservation Policy*, INSIGHTSIAS (Dec. 26, 2016), <http://www.insightsonindia.com/2016/12/26/insights-editorial-karnatakas-dangerous-new-reservation-policy/> [<http://perma.cc/MT84-Y7NG>].

<sup>31</sup> INDIA CONST. art. 15, § 2.

<sup>32</sup> *Id.* at art. 15, § 4.

<sup>33</sup> *Id.* at art. 16, § 2.



to residence within that State or Union territory prior to such employment or appointment.<sup>34</sup>

This provision enables the Parliament to carve out an exception to Article 16's non-discrimination mandate based on residence. However, state governments have in the past enacted laws without parliamentary authorization and/or in the absence of a parliamentary enactment permitting them to do so, pursuing policies of localism. The Parliament has exercised very little control over these policies. Parliament enacted the Public Employment (Requirement as to Residence) Act, 1957 that abolished all existing residence requirements in various states and provided for exceptions only in the case of the special instances of Andhra Pradesh, Manipur, Tripura, and Himachal Pradesh.<sup>35</sup> This means that the central government has only given the aforementioned states the right to issue directions for setting residence requirements. Yet, as Justice P.N. Bhagwati of the Supreme Court of India has rightly pointed out,

[S]ome of the states are adopting "sons of the soil" policies prescribing reservation or preference based on domicile or residence requirement for employment or appointment to an office under the government of a State or any local or other authority or public sector corporation or any other corporation which is an instrumentality or agency of the State.<sup>36</sup>

In *State of Jammu & Kashmir v. Triloki Nath Khosa & Ors*,<sup>37</sup> the court held that equality of opportunity under Article 16 for any office under the state is done by meeting the necessary qualifications and further, based on capability. This does not act as an impediment to the state prescribing necessary qualifications and tests for selection and recruitment for government services. Also, the Article applies to employment and offices under the state (and subordinates to the state). The state is also an authority to lay down conditions of appointment that include "mental excellence, . . . physical fitness, sense of discipline, moral integrity and loyalty to state."<sup>38</sup>

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<sup>34</sup> *Id.* at art. 16, § 3.

<sup>35</sup> See generally Public Employment Act, No. 44 of 1957 (India), <https://indiankanoon.org/doc/67961/> [<http://perma.cc/5HGS-XND8>].

<sup>36</sup> Dr. Pradeep Jain v. Union of India, (1984) 3 SCR 932, 956–57 (India).

<sup>37</sup> State of Jammu & Kashmir v. Triloki Nath Khosa, (1974) 1 SCR 771, 790 (1973) (India).

<sup>38</sup> Dipti Khatri, *Equality of Opportunity in Public Employment*, ACADEMIKE (Jan. 12, 2015), [https://www.lawctopus.com/academike/equality-opportunity-public-employment/#\\_edn4](https://www.lawctopus.com/academike/equality-opportunity-public-employment/#_edn4) [<http://perma.cc/TUB2-6L34>]; see generally MAHENDRA P. SINGH, V. N. SHUKLA'S CONSTITUTION OF INDIA (11th ed. 2008).

### 1. Concerns before the Supreme Court of India

The foremost concern before the Supreme Court of India was determining the correct method of the allocation requirement of the reserve category based on the respective state rule. However, since the pertinent issue here is the validity of basing employment opportunities on domicile, relevant Indian Supreme Court cases will be analyzed. In *Kailash Chand Sharma v. State of Rajasthan And Others*,<sup>39</sup> the concern emerged regarding the advantage in public employment based on the rural/urban divide. This case was brought before the Supreme Court of India with a challenge against a Circular dated June 10, 1998, issued by the Department of Rural Development and Panchayat Raj dealing with the procedure to be followed for appointment of teachers during the years 1993 to 1999 by way of direct recruitment and is as follows:

Fixation of Bonus Marks for Domiciles <sup>40</sup>	
Domiciles of Rajasthan	10 Marks
Resident of District	10 Marks
Resident of Rural Area of District	5 Marks

It is relevant that the relaxation of marks was in the Higher Secondary School and had an impact on the candidates as there was no written examination and selection was based on an interview.<sup>41</sup>

The contentions by the state government were based on geographical classification and the socio-economic backwardness of the area.<sup>42</sup> The state government argued that residence of a district or rural area would be a good classification for selection in public employment.<sup>43</sup> The state reasoned that villages and towns are backward educationally and economically and that teachers recruited from urban or forward districts are not desirous of teaching in rural areas and relatively backward districts.<sup>44</sup> Concerns about teacher absenteeism, a pressing issue in Indian government school, was also put forth as a reason for giving preference to persons living in the same area to be recruited as teachers.<sup>45</sup> The court noted that none of the

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<sup>39</sup> *Kailash Chand Sharma v. State of Rajasthan And Ors.*, AIR 2002 SC 2877, para. 33 (India).

<sup>40</sup> *Id.* at paras. 4–5.

<sup>41</sup> *Id.* at para. 6.

<sup>42</sup> *Id.* at para. 14.

<sup>43</sup> *Id.* at para. 35.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

assumptions by the state government were based upon concrete material or data, and that it cannot be presumed that all states, villages, and towns are backward educationally or economically.<sup>46</sup> The court did not find strength in the argument that the differentia based on domicile was to encourage vernacular language that was to be taught by the teachers at the primary level to students and that a teacher from a village having the same dialect will be able to teach the students of the same district better.<sup>47</sup> The court found that:

[U]ndue accent is being laid on the dialect theory without factual foundation. The assertion that dialect and nuances of the spoken language varies from district to district is not based upon empirical study or survey conducted by the State. Not even specific particulars are given in this regard. The stand in the counter-affidavit . . . is that “each zone has its distinct language.”<sup>48</sup>

The court correctly emphasized that if the state government wanted to remedy these defects, steps should have been taken to notify a language requirement for candidates to apply and not make categorization based on domicile. The court stated that this notification has “overtones of parochialism [and] is liable to be rejected on the plain terms of Article 16(2) and in the light of Article 16(3).”<sup>49</sup> The court went on to further state that “[a]n argument of this nature flies in the face of the peremptory language of Article 16(2) and runs counter to our constitutional ethos founded on unity and integrity of the nation.”<sup>50</sup>

The correct interpretation of Article 16 was mentioned in *Jagdish Negi v. State of U.P.*, wherein the hill and Uttarakhand areas in the State of Uttar Pradesh were taken to be correct instances of socially and educationally backward classes of citizens, and thereby received a twenty-seven percent reservation benefit.<sup>51</sup> The court upheld this reservation benefit under Article 16 because the state reservations were reasonable based on all legitimate claims and relevant factors.<sup>52</sup>

In *State of Maharashtra v. Raj Kumar*, the State of Maharashtra promulgated a rule with a residential condition for employment within the state.<sup>53</sup> To be given the advantage of a “rural candidate,” the examinee must be from a town or village

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<sup>46</sup> *Id.* at para. 37.

<sup>47</sup> *Id.* at para. 36.

<sup>48</sup> *Id.*

<sup>49</sup> *Id.* at para. 14.

<sup>50</sup> *Id.*

<sup>51</sup> *Jagdish Negi v. State of U.P.*, AIR 1997 SC 3505, para. 15 (India).

<sup>52</sup> *Id.* at para. 16.

<sup>53</sup> AIR 1982 SC 1301, 1301 (India).

having type “C” municipality so that knowledge of rural life and its problems are known to the candidate and hence the candidate will be more suitable for the job that entails work in rural areas. The court struck down this rule and held it to be violative of Articles 14 and 16 of the Constitution of India.<sup>54</sup> The court stated that there was “no nexus between the classification” that the state government made and “the object that [was] sought to be achieved . . . [since] as the Rule stands any person who may not have lived in a village at all can appear for S.S.C. Examination . . . [and] become eligible for selection . . . .”<sup>55</sup>

In *A.V.S. Narasimha Rao v. State of Andhra Pradesh*,<sup>56</sup> a constitutional bench of the Supreme Court of India looked into a law enacted by the Parliament under Article 16(3) of the Constitution of India and the enabling power under Section 3 of the Public Employment Act.<sup>57</sup> Domicile preference in public employment was provided to the Telengana region of the State of Andhra Pradesh.<sup>58</sup> A fifteen-year continuous residency was required.<sup>59</sup> The court held the Act was ultra vires of the Constitution of India by stating that even if enacted by the Parliament, the court must follow the constitution’s vision of equality in employment, and that unless advancements are to be made for less developed states, the structure provided under Article 16 cannot be disturbed.<sup>60</sup>

Many of the Supreme Court of India’s cases analyzing the issue of domicile preference in public employment deal with a peculiar scenario—the state governments have repeatedly faltered in deciphering a way to calculate the intricacies of deriving how many seats make up the reservation scheme. The Supreme Court of India discussed the allocation in cases based on women that was to be applicable to issues relating to horizontal reservation. In this regard, the Supreme Court of India in *Indra Sawhney v. Union of India*, discussed all constitutional provisions pertaining to reservations;<sup>61</sup> it also discussed the principle of horizontal reservation, stating:

[A]ll reservations are not of the same nature. There are two types of reservations, which may, for the sake of convenience, be referred to as “vertical reservations” and “horizontal reservations”. The reservations in favour of Scheduled Castes, Scheduled Tribes and other backward

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<sup>54</sup> *Id.*

<sup>55</sup> *Id.*

<sup>56</sup> (1970) 1 SCR 115, 117 (India).

<sup>57</sup> *Id.* at 119.

<sup>58</sup> *Id.* at 116.

<sup>59</sup> *Id.* at 118.

<sup>60</sup> *Id.* at 121.

<sup>61</sup> AIR 1993 SC 477, 556 (India).

classes (under Article 16(4) may be called vertical reservations whereas reservations in favour of physically handicapped (under clause (1) of Article 16) can be referred to as horizontal reservations. Horizontal reservations cut across the vertical reservations — what is called inter-locking reservations. To be more precise, suppose 3% of the vacancies are reserved in favour of physically handicapped persons; this would be a reservation relatable to clause (1) of Article 16. The persons selected against this quota . . . will be placed in that quota by making necessary adjustments; similarly, if he belongs to open competition (O.C.) category, he will be placed in that category by making necessary adjustments. Even after providing for these horizontal reservations, the percentage of reservations in favour of backward class of citizens remains — and should remain — the same.<sup>62</sup>

In *Anil Kumar Gupta v. State of U. P.*, the Supreme Court of India examined the question of distribution of seats under the concept of horizontal reservation and went on to clarify the proper procedure for determination of horizontal reservation:<sup>63</sup>

Now, coming to the correctness of the procedure prescribed by the revised notification for filling up the seats, it was wrong to direct the fifteen per cent special reservation seats to be filled up first and then take up the OC (merit) quota (followed by filling of OBC, SC and ST quotas). The proper and correct course is to first fill up the OC quota (50%) on the basis of merit; then fill up each of the social reservation quotas, i.e., SC, ST and BC; the third step would be to find out how many candidates belonging to special reservations have been selected on the above basis. If the quota fixed for horizontal reservations is already satisfied — in case it is an overall horizontal reservation — no further question arises. But if it is not so satisfied, the requisite number of special reservation candidates shall have to be taken and adjusted/accommodated against their respective social reservation categories by deleting the corresponding number of candidates therefrom. (If, however, it is a case of compartmentalised horizontal reservation, then the process of verification and adjustment/accommodation as stated above should be applied separately to each of the vertical reservations. In such a case, the reservation of fifteen percent in favour of special categories, overall, may be satisfied or may not be satisfied.)<sup>64</sup>

This judgment has been followed in *Rajesh Kumar Daria v. Rajasthan Public Service Commission*,<sup>65</sup> where the court looked into the different modes of calculating horizontal and vertical reservation and held that persons belonging to a reserved category and appointed to non-reserved posts on their own merit cannot be counted against the reserved quota in the case of vertical

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<sup>62</sup> *Id.*

<sup>63</sup> *Anil Kumar Gupta v. State of U.P.*, (1995) 5 SCC 173, 185 (India).

<sup>64</sup> *Id.* at 185.

<sup>65</sup> AIR 2007 SC 3127, 3129–30 (India).

reservation.<sup>66</sup> This case further elucidated that the principle would not be applicable for horizontal reservation and observed:

The second relates to the difference between the nature of vertical reservation and horizontal reservation. Social reservations in favour of SC, ST and OBC under Art[icle] 16(4) are “vertical reservations”. Special reservations in favour of physically handicapped, women, etc., under Art[icle] 16(1) or 15(3) are “horizontal reservations”. Where a vertical reservation is made in favour of a backward class under Art[icle] 16(4), the candidates belonging to such backward class, may compete for non-reserved posts and if they are appointed to the non-reserved posts on their own merit, their numbers will not be counted against the quota reserved for respective backward class. Therefore, if the number of SC candidates, who by their own merit, get selected to open competition vacancies, equals or even exceeds the percentage of posts reserved for SC candidates, it cannot be said that the reservation quota for SCs has been filled. The entire reservation quota will be intact and available in addition to those selected under Open Competition category. But the aforesaid principle applicable to vertical (social) reservations will not apply to horizontal (special) reservations. Where a special reservation for women is provided within the social reservation for Scheduled Castes, the proper procedure is to first to fill up the quota for Scheduled Castes in order of merit and then find out the number of candidates among them who belong to the special reservation group of “Scheduled Castes-Women”. If the number of women in such list is equal to or more than the number of special reservation quota, then there is no need for further selection towards the special reservation quota. Only if there is any shortfall, the requisite number of Scheduled Caste women shall have to be taken by deleting the corresponding number of candidates from the bottom of the list relating to Scheduled Castes. To this extent, horizontal (special) reservation differs from vertical (social) reservation. Thus women selected on merit within the vertical reservation quota will be counted against the horizontal reservation for women.<sup>67</sup>

The Supreme Court of India, while examining the state government notification on horizontal reservation, went on to clarify the percentage of reservation in favor of this reserved class. As mentioned above, in *Indra Sawhney*, the Supreme Court of India stated that the total person recruited should not exceed fifty percent of the reservation.<sup>68</sup> This also applies to horizontal reservation. Hence, candidates under horizontal reservation under Article 16(4) of the Constitution of India

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<sup>66</sup> *Id.* at 3130.

<sup>67</sup> *Id.* (internal citations omitted).

<sup>68</sup> *Id.* at para. 5.



should not exceed the fifty percent reservation.<sup>69</sup> The foray of regionalism in India, the emergence of parochial loyalties with the rise and growth of numerous regional political parties, and the advantages that these political parties want to gain for themselves are influencing governments to make campaign commitments for quota based on domicile and have found inroads via these state government notifications. The Supreme Court of India observed that these parties utilize domicile reservations with a “view to gaining advantage for themselves,”<sup>70</sup> and that this results in “a serious threat . . . to the unity and integrity of the nation and [puts] the . . . concept of India as a nation . . . in peril.”<sup>71</sup> The court emphasized that the spirit of nationhood and the “sons of the soil” are not populist demands and are not appeals to be made that are

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<sup>69</sup> See Hon. Mr. J. S. Nagamuthu, *K.R. Shanthy v. Sec’y to Gov’t*, MADRAS HIGH COURT, para. 14 (Oct. 1, 2012) (India), <http://indiankanoon.org/doc/41866200> [<http://perma.cc/LQ32-NU56>]. The High Court laid out the process to be used:

First Step:

- (i) As against the number of vacancies identified for open quota, irrespective of caste, sex, physically challenged, etc., everyone should be allowed to compete based on merits.
- (ii) The meritorious candidates should be first selected as against the above vacancies under open quota.

Second Step:

- (iii) After completing the first step, moving on to the vertical reservation categories, selection has to be made for each category from amongst the remaining candidates belonging to the particular reserved category (vertical) based on merits.

Third Step:

- (iv) After completing the second step, horizontal reservation which cuts across the vertical reservation has to be verified as to whether the required number of candidates who are otherwise entitled to be appointed under the horizontal reservation have been selected under the vertical reservation.
- (v) On such verification, if it is found that sufficient number of candidates to satisfy the special reservation (horizontal reservation) have not been selected, then required corresponding number of special reservation candidates shall have to be taken and adjusted/accommodated as against social reservation categories by deleting the corresponding number of candidates therefrom.
- (vi) Even while filling up the vacancies in the vertical reservation, if, sufficient number of candidates falling under the horizontal reservation have been appointed, then, there will be no more appointment exclusively under the horizontal reservation.

Caution:

- (vii) At any rate, the candidates who were selected as against a post under open quota shall not be adjusted against the reserved quota under vertical reservations.

*Id.*; see also CAV Order at para. 19, High Court of Chhattisgarh, Bilaspur (2015) (W.P.(S) Nos. 869/2015, 870/2015, 871/2015 & 1477/2015) (India), <http://cghighcourt.nic.in/Afr/courtJudgementandAFR/2016/Jan/wps869of2015.pdf> [<http://perma.cc/X3KA-459B>]; J. Venkatesan, *Quota should not exceed 50%, says Supreme Court*, THE HINDU (last updated Oct. 9, 2016), <https://www.thehindu.com/todays-paper/tp-national/Quota-should-not-exceed-50-says-Supreme-Court/article15210960.ece> [<http://perma.cc/FS5A-JDVL>].

<sup>70</sup> Dr. Pradeep Jain v. Union of India, (1984) 3 SCR 942, 955 (India).

<sup>71</sup> *Id.*

contrary to the constitution.<sup>72</sup> The Supreme Court of India has also warned that special treatment on the basis of residence is not to be utilized as a populist appeal by the political parties that can break “the unity and integrity of the nation by fostering and strengthening narrow parochial loyalties based on language and residence within a state.”<sup>73</sup>

Hence, a permanent resident in a state should not entertain the feeling of a preferential claim for appointment opportunity into the state government as against another person who is deemed to be an outsider, especially irrespective of merit.<sup>74</sup> The Supreme Court of India has rightfully stated that this “is a dangerous feeling [and] if allowed to grow . . . might one day break up the country into fragments,”<sup>75</sup> reasonable preferential policy based on rationale, notwithstanding.

The Constituent Assembly Debates (CAD) peaks a similar tone by mentioning that India offers only one citizenship, thereby making no distinction between residents of various states, and hence there should be an “unfettered right and privilege of employment” in any part of the country.<sup>76</sup> The members present at the CAD, however, expressed concern that persons from any state should not be allowed to come from one province to another, “as mere birds of passage without any roots, without any connection with that particular province, just to come, apply for posts and, so to say, take the plums and walk away.”<sup>77</sup> And that there should be certain limitations that are necessary. The CAD also addressed the issue of giving Parliament the power of bringing about uniformity to the residential limits in the states.

On a side note, in Indian cases involving educational institutions and admissions to higher educational institutions, the domicile privilege is abundant. However, the recent jurisprudence in super specialized courses has changed by not allowing domicile reservations.<sup>78</sup>

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<sup>72</sup> *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *See id.*

<sup>75</sup> *Id.*

<sup>76</sup> CONSTITUENT ASSEMBLY DEBATES, 7 THE CONSTITUENT ASSEMBLY OF INDIA 676 (Nov. 30, 1949).

<sup>77</sup> *Id.* at 700.

<sup>78</sup> *See Dr. Pradeep Jain*, 3 SCR at 951; *see also* Mukesh Kumar Umar v. State of Madhya Pradesh, WP No. 2377/2018, para. 4 (Madhya Pradesh HC, Mar. 7, 2018) (India), <https://indiankanoon.org/doc/165550674/> [<http://perma.cc/D7KK-GX3F>] (contending that there “cannot be any discrimination on the basis of place of birth or residence for a [sic] public employment but place of residence can be considered for admission to the professional colleges”).

## 2. Concerns before Various High Courts

In *Mukesh Kumar Umar v. State of Madhya Pradesh*<sup>79</sup> a division bench decision of the High Court of Madhya Pradesh examined a government notification for the recruitment of assistant professors that had a substantial upper age requirement relaxation for candidates domiciled within the state of Madhya Pradesh.<sup>80</sup> The upper age limit for candidates domiciled in Madhya Pradesh was forty-years old, whereas for candidates domiciled outside Madhya Pradesh, the upper age limit was between twenty-one to twenty-eight years.<sup>81</sup> In the return filed, the state has referred to Madhya Pradesh Educational Service (Collegiate Branch) Recruitment Rules, 1990 subsequently amended, whereby the upper age limit was contemplated to be as admissible in accordance with the directions/instructions issued by the General Administration Department of the state government from time to time.<sup>82</sup> The notification specifically stated that the relaxation in the maximum age limit shall not be granted to candidates from outside the state.<sup>83</sup> The rationale was that there were no recruitments that could take place in the state since the year 1993 and hence the residents of the State of Madhya Pradesh would be at a disadvantage if the posts were kept open to competition from candidates from all over India.<sup>84</sup> The court held that there cannot be different age limits based only on place of birth or place of residence, and that the fault lay with the Government of Madhya Pradesh for not conducting timely appointments without prolonged gaps in time.<sup>85</sup> The court found that the state government's rationale for the regulation had no genesis in the constitution.<sup>86</sup> The court went on to further reason that if the state is unable to make appointments for a number of years then it is the state alone, which has to be blamed.<sup>87</sup> The court found:

[T]he Constitutional mandate of providing equality of opportunity and no discrimination on the basis of place of residence or place of birth cannot be permitted to be given a go-bye only for the reason that the State was not able to conclude the employment process in the State for large number of years.<sup>88</sup>

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<sup>79</sup> *Mukesh Kumar Umar*, WP No. 2377/2018 at paras. 3–4.

<sup>80</sup> *Id.*

<sup>81</sup> *Id.* at paras. 1, 3 (“As per Circular No. C 3-8/2016/3-1, May 12, 2017, General Administration Department.”).

<sup>82</sup> *Id.* at para. 2.

<sup>83</sup> *Id.* at para. 3.

<sup>84</sup> *Id.* at para. 8.

<sup>85</sup> *Id.* at para. 13.

<sup>86</sup> *Id.* at paras. 12–13.

<sup>87</sup> *Id.*

<sup>88</sup> *Id.* at para. 13.

In *Smt. Prabha Ranjan Gupta v. The State Of Jharkhand And Ors*, the court had to determine the selection of candidates, considering that as part of the same advertisement a few years before the initiation of a new advertisement, few candidates were appointed.<sup>89</sup> Hence, the 0.06% percent reservation—though accepted by an earlier Supreme Court of India decision as equivalent to one post—was held not applicable in this case as certain candidates were already appointed earlier.<sup>90</sup> Also, the court pointed out the role of domicile in the five percent reservation for women is applicable only for domiciles of the State of Jharkhand.<sup>91</sup> This appeal was dismissed eventually, as the Petitioner had obtained only the minimum qualifying marks, which cannot create any right of appointment upon the candidate.<sup>92</sup> In *Hemanand Mani Tripathi v. State of Chhattisgarh*,<sup>93</sup> age relaxation provided to candidates of the State of Chhattisgarh was asked to be reconsidered by the Petitioners. The State of Chhattisgarh argued that the relaxation to candidates of Chhattisgarh for recruitment to the State Civil Services was based, not only on residence, but on a host of categories.<sup>94</sup> The court held that candidates from other states were not barred from writing the examination and are eligible to apply for the posts advertised, provided they conform to the eligibility criteria prescribed under the Examination Rules.<sup>95</sup> So while the age relaxation was not interfered with, the court, nevertheless, directed the state to consider all those candidates who become ineligible because of age limit in the next recruitment process, with the liberty to choose other remedies.<sup>96</sup>

In other cases, different concerns have been added to the domicile question. The Union Territory of Pondicherry adopted a policy of the central government where all Scheduled Castes or Scheduled Tribes, are eligible for posts reserved for Scheduled Castes/Scheduled Tribes candidates, irrespective of their domiciled state which was upheld by the court.<sup>97</sup> The court held that “no legal infirmity can be ascribed to such a policy and the same cannot be held to be contrary to any provision of law.”<sup>98</sup>

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<sup>89</sup> *Smt. Prabha Ranjan Gupta v. The State Of Jharkhand & Ors.*, (2014) 3 J.L.J.R. 204, para. 3 (India).

<sup>90</sup> *See id.*

<sup>91</sup> *Id.* at para. 16 (basing its analysis in view of the letter No. 5448 dated 12.9.2011 of Personnel, Administrative Reforms and Official Languages Department).

<sup>92</sup> *See generally id.*

<sup>93</sup> W.P. (S) No. 40856/2009, Chhattisgarh High Court (2010), [https://www.keralapsc.gov.in/index.php?option=com\\_docman&task=doc\\_view&gid=20470&Itemid=15](https://www.keralapsc.gov.in/index.php?option=com_docman&task=doc_view&gid=20470&Itemid=15) [<http://perma.cc/Ez38-KCK6>].

<sup>94</sup> *See generally id.*

<sup>95</sup> *See generally id.*

<sup>96</sup> *See generally id.*

<sup>97</sup> *S. Pushpa v. Sivachanmugavelu*, AIR 2005 SC 1038, 1038 (India).

<sup>98</sup> *Id.*

A similar question presented itself before a full bench at the Delhi High Court, where the court examined whether in Union Territories, notifications for government employment can include Scheduled Castes from other states.<sup>99</sup> The court based its decision on an important observation that, “unlike in the case of States, Union Territories are within the administrative control of the Union Government.”<sup>100</sup> It follows that any Scheduled Caste or Scheduled Tribe notified by the president, based on the description, would be entitled to the benefit of reservation in all Union Territories.<sup>101</sup> However, as mentioned in the Constitution of India, states have a different administrative arrangement, and hence the position as mentioned for the Union Territories would not apply and migrations between states would disentitle a person from applying to a government position (if tested for constitutional validity).<sup>102</sup> The court allowed Scheduled Caste and Scheduled Tribe candidates from other states to avail relevant reservation benefits for jobs in Delhi.<sup>103</sup>

## II. THE UNITED STATES

In the United States, the principle of equality in employment is followed, except in the case of public contracts that have sought concessions from the government. This distinction is relevant for this Article as the capitalist regime in the U.S. supports outsourcing all public works, which differs from the socialistic nature of the Constitution of India reflected in its economy. Further, the Privileges and Immunities Clause of Article IV, Section 2, Clause 1 of the U.S. Constitution provides that “the citizens of each state shall be entitled to all Privileges and Immunities of citizens in the several states.”<sup>104</sup> Also known as the interstate privileges and immunities clause, this provision ensures to “a citizen of State A who ventures into State B the same privileges which the citizens of State B enjoy.”<sup>105</sup> In a federal structure of government, the Privileges and Immunities Clause helps “fuse into one Nation a collection of independent, sovereign States.”<sup>106</sup>

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<sup>99</sup> Deepak Kumar v. District and Sessions Judge, Delhi (2013) 1, Part 2 I.L.R. 519, 524 (2012) (India).

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> *Id.* at 547–48.

<sup>103</sup> Jayant Sriram, *SC/ST from other states eligible for Delhi govt job quota: HC*, INDIAN EXPRESS (Sept. 14, 2012, 12:33 AM), <https://indianexpress.com/article/india/india-others/sc-st-from-other-states-eligible-for-delhi-govt-job-quota-hc/> [http://perma.cc/7GF9-X5CG].

<sup>104</sup> U.S. CONST. art. IV, § 2, cl. 1.

<sup>105</sup> Toomer v. Witsell, 334 U.S. 385, 395 (1948).

<sup>106</sup> *Id.*

The U.S. Constitution also contains the Commerce Clause, which gives the federal government the power “[t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes. . .”<sup>107</sup> Additionally, the dormant Commerce Clause, a judicial construction read into the Commerce Clause, prohibits discrimination or excessive burdens on interstate commerce. The Privileges and Immunities Clause and the Commerce Clause both lend themselves to the analysis of employment and interstate regulation, as discussed below.

The first issue to be addressed by the Court regarding employment equality was whether the movement of persons is “commerce” under the interstate Commerce Clause, which was confirmed in multiple cases, such as *Gloucester Ferry Co. v. Pennsylvania*<sup>108</sup> and *Edwards v. California*.<sup>109</sup> Subsequently, *Brown v. Anderson* noted that a state regulation that adversely restricts the interstate flow of labor burdens commerce and may violate the Commerce Clause and the Privileges and Immunities Clause.<sup>110</sup> In short, the movement of commerce and any restriction therein may become a burden on commerce, and once shown to exist, the next question to be looked at is whether it is constitutionally tolerable to take on the local interest.<sup>111</sup> To survive constitutional scrutiny, it is not enough for the state to show that it is advancing its own economic interest.

Another case, *Hicklin v. Orberk*,<sup>112</sup> dealt with Alaska’s local hiring plan (Alaska Local Hire Act), which infringed on nonresidents’ right to work. The central argument in the case was that such infringement went against the fundamentals of the Privileges and Immunities Clause.<sup>113</sup> The state responded that the Privileges and Immunities Clause does not apply to the right to work, especially when the resources and property of the state were utilized, and that the Alaska Local Hire Act did not violate the Clause under the appropriate standard of review.<sup>114</sup> The Supreme Court unanimously held that the Alaska Local Hire Act violated the Constitution.<sup>115</sup> Analyzing past decisions, Justice Brennan stated that the Alaska Local Hire Act does not meet the strict standards of the Privileges and Immunities Clause,

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<sup>107</sup> U.S. CONST. art. I, § 8, cl. 3.

<sup>108</sup> 114 U.S. 196, 203 (1885).

<sup>109</sup> 314 U.S. 160, 172 (1941) (“[I]t is settled beyond question that the transportation of persons is ‘commerce’, within the meaning of [the Commerce Clause].”).

<sup>110</sup> 202 F. Supp. 96, 101–03 (D. Alaska 1962).

<sup>111</sup> *See id.* at 102–03.

<sup>112</sup> 437 U.S. 518, 520 (1978).

<sup>113</sup> *Id.* at 520–21, 523.

<sup>114</sup> *Id.* at 528.

<sup>115</sup> *See id.* at 534.



especially since there was no evidence of non-citizens being a peculiar source of evil or a major cause of state unemployment.<sup>116</sup>

*Hicklin* is not the first case to deal with these issues. For example, *Corfield v. Coryell* dealt with a New Jersey regulation limiting the right to fish from New Jersey water to its own citizens.<sup>117</sup> The court agreed with the legislation, resting its argument on New Jersey's need to protect its depleting natural resources and ensure that its supply of shell fish was available to New Jersey citizens for their benefit.<sup>118</sup> In *McCready v. Virginia*, a nonresident challenged Virginia legislation that denied him the right to plant oysters in the state.<sup>119</sup> The Court upheld the legislation and based its argument on the fact that the citizens of Virginia and its government owned the land and hence, had the power to dispose of those areas vested with them.<sup>120</sup> Further, the Court stated that the ownership of property in a state, held in common by all the citizens of a particular state was:

[N]ot a privilege and immunity of general [citizenship] but of special citizenship. It does "not belong of right to the citizens of all free governments," but only to the citizens of Virginia, on account of the peculiar circumstances in which they are placed. . . . They owned it, not by virtue of citizenship merely, but of citizenship and domicile united; that is to say by virtue of a citizenship confined to that particular locality.<sup>121</sup>

In the landmark case of *Toomer v. Witsell*,<sup>122</sup> the Court set forth what has become the modern Privileges and Immunities doctrine. *Toomer* involved a South Carolina statute that discriminated against nonresident commercial shrimp fishermen by imposing a license fee 100 times greater than that charged to residents.<sup>123</sup> The Court declared the statute invalid and violative of the Privileges and Immunities Clause by stating that "[t]he whole ownership theory, in fact, is now generally regarded as but a fiction expressive in legal shorthand of the importance to its people that a State have power to preserve and regulate the exploitation of an important resource."<sup>124</sup> Furthermore, the Court reasoned, "[b]y that statute, South Carolina plainly and frankly discriminates against non-residents, and the record leaves little doubt but what the discrimination is so great that its practical effect is virtually

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<sup>116</sup> *Id.* at 527–28.

<sup>117</sup> *See Corfield v. Coryell*, 6 F. Cas. 546, 549 (C.C.E.D. Pa. 1823) (No. 3230).

<sup>118</sup> *See id.* at 552.

<sup>119</sup> *McCready v. Virginia*, 94 U.S. 391, 392 (1876).

<sup>120</sup> *See id.* at 395–96.

<sup>121</sup> *Id.* at 396.

<sup>122</sup> 334 U.S. 385, 395–403 (1948).

<sup>123</sup> *Id.* at 395.

<sup>124</sup> *Id.* at 402.

exclusionary.”<sup>125</sup> Expanding on *Toomer*, a later court stated that “the [C]lause seeks to prevent discrimination against nonresidents, to further the concept of federalism, and to create a national economic unit.”<sup>126</sup>

The Court in *Toomer* emphasized that each state had to accord substantial equality of treatment to the citizens of the other, and developed a two-prong test, which prohibited a state from discriminating against nonresidents unless (1) there is substantial reason for the difference in treatment, and (2) the discriminatory remedy bears a close relation to the state’s objective.<sup>127</sup>

This is not to say that all kind of restrictions are unconstitutional and objectionable. Some of the restrictions for bona fide residence requirements for state or municipal employment might be acceptable. However, serious objections arise when a domicile preference expands into the private sector. This is where the *Toomer* Privileges and Immunities Clause test would come into play to raise objections to the unnecessary relegation of nonresidents to last in hiring priority.

Hence, the investigation that a court has to make in each case is whether reasons exist for establishing discriminatory policies, and whether the degree of discrimination bears a close relation to them. The inquiry must also, of course, be conducted with due regard for the principle that the states should have considerable leeway in analyzing local evils and in prescribing appropriate cures. “Although the Commerce Clause speaks only in broad terms of giving Congress authority to ‘regulate commerce . . . among the several states’, the Supreme Court has often invoked the [C]lause to strike down state legislation that unreasonably impedes the flow of commerce across state lines.”<sup>128</sup> In other words, the Court has applied the Commerce Clause to state and municipal enactments that unreasonably burdened interstate commerce.<sup>129</sup>

Observing the argument put forth by the states in these cases, which revolves around the “common property” of the state, it can seem to be illusionary since it is more the case of preserving employment by closing the same opportunities to nonresidents. In the context of the state, regardless of whether the ingredient of employment—for example, fishing—can constitute the common

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<sup>125</sup> *Id.* at 397.

<sup>126</sup> *Sheley v. Alaska Bar Ass’n*, 620 P.2d 640, 642 (Alaska 1980).

<sup>127</sup> *See Toomer*, 334 U.S. at 398–99.

<sup>128</sup> *United Bldg. & Constr. Trades Council v. Camden*, 88 N.J. 317, 338 (1982) (citing U.S. CONST. art. I, § 8).

<sup>129</sup> *See Dean Milk Co. v. Madison*, 340 U.S. 349, 350, 353 (1951).

property of the state, it is not an acceptable argument to say that a state can “own” any employment. Hence, the restriction analyzed in *McCready*, for example, rightfully lacks a justifying rationale when a state attempts to limit employment to its own citizens.

With the passage of time, interpretations continue to lean towards invalidating statutes that are prohibitive and restrictive of the Privileges and Immunities Clause and the Commerce Clause. For example, in *Douglas v. Seacoast Products, Inc.*,<sup>130</sup> the Court—while looking at a Virginia law prohibiting vessels owned by nonresidents from fishing in Chesapeake Bay—held that “it [was] pure fantasy to talk of ‘owning’ wild fish, birds, or animals . . . [u]nder modern analysis, the question is simply whether the State ha[d] exercised its police power in conformity with the federal laws and Constitution.”<sup>131</sup> Interestingly, it was not the right to purchase, but the right to plant—as in the case of Virginia—and not the right to buy, but to extract that was being challenged in the aforementioned cases.

Like in India, there are cases in the United States that look at the Privileges and Immunities Clause and the Commerce Clause in a different light. In *Hughes v. Alexandria Scrap*, the United States Supreme Court determined that “[n]othing in the purposes animating the Commerce Clause prohibits a State, in the absence of congressional action, from participating in the market and exercising the right to favor its own citizens over others.”<sup>132</sup> Similarly, in *Reeves, Inc. v. Stake*,<sup>133</sup> the Court held that the South Dakota Cement Commission did not violate the Commerce Clause through its decision to give state buyers an absolute preference in fulfilling their requirements for cement in times of shortage. “Restraint in this area is also counseled by considerations of state sovereignty, the role of each State ‘as guardian and trustee for its people,’ and ‘the long recognized right of trader or manufacturer . . . to exercise his own independent discretion as to parties with whom he will deal.’”<sup>134</sup> The Court said that the principle of the state, as a market participant, has the freedom to favor its own citizens and choose the parties with whom it will deal. Other courts have also “noted that a state’s ‘purchase of goods and materials for its own end use . . . is not subject to the usual Commerce Clause restrictions.’”<sup>135</sup> However, “[t]he mere

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<sup>130</sup> 431 U.S. 265, 284–85 (1977).

<sup>131</sup> *Id.*

<sup>132</sup> *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 810 (1976).

<sup>133</sup> 447 U.S. 429, 446–47 (1980).

<sup>134</sup> *Id.* at 436, 438 (citing *Heim v. McCall*, 239 U.S. 175, 191 (1915); quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)).

<sup>135</sup> *United Bldg. & Constr. Trades Council v. Camden*, 88 N.J. 317, 339 (1982) (citing *K.S.B. Tech. Sales v. N. Jersey Dist. Water Supply*, 75 N.J. 272 (1977)).

fact that it was through its leasing power that Alaska infringed the [P]rivileges and [I]mmunities and [I]nterstate [C]ommerce [C]lauses does not save the Alaska Hire Act from its constitutional infirmities.”<sup>136</sup>

Another relevant point here is that the Alaska Local Hire Act did not apply to private employment or all sectors of oil and gas employment, and, thus, the Act has a small impact on the nation’s labor pool. Attention has to be drawn to the fact that the Act reaches only oil and gas work on state-leased property or jobs that are directly related. It might be further argued that the domicile status that is available to anyone willing to establish it depends on the duration of residence and intention to stay. However, one must establish this domicile, which is not burden-free. More so, the nonresident migrant has to forfeit benefits of citizenship of the former state. Then the questions of intent remain: Does he intend to make his new residence his permanent residence? It is in this light that a residency preference might restrict the flow of labor to the extent that persons might be so deterred that even the most qualified among them might look elsewhere for jobs, thereby interfering with maximization of productivity of the state that enacted these restrictions. This would, in turn, impact the economy of the concerned state, and eventually discourage investment. Thus, these principles of restrictive hire place a burden on interstate commerce. The question then becomes this: Whether local interests outweigh this burden.<sup>137</sup>

### CONCLUSION

The past cases show the need to engage in conversations about a valid reason for encouraging a type of state discrimination that will not encroach upon the strict scrutiny required under the Equal Protection Clause, and can remain exclusively under the Court’s Privileges and Immunities and Commerce Clause jurisprudence.

As with most constitutional guarantees, the Privileges and Immunities Clause and the Commerce Clause are not absolute. States may continue to distinguish between citizens and non-citizens so long as there is a valid and substantial reason for so doing. This principle has also been upheld in Indian courts. Judicial intervention is necessary to make sure that any extreme use of local hiring by a state is not practiced in a manner that would result in its interference—especially in today’s time—in the

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<sup>136</sup> Carl J. Schuman, *Domicile Preferences in Employment: The Case of Alaska Hire*, DUKE L.J. 1069, 1092 (1978).

<sup>137</sup> *Id.* at 1085–89.

private sector. Such a result might be a retaliatory use of local hiring preferences, producing a “Balkanization of interstate commercial activity which the Constitution was intended to prevent,”<sup>138</sup> an ideal contrary to the constitutional vision of the forms of government. This is in consonance with what the United States Supreme Court and the Supreme Court of India have stressed: A division on state lines so as to destroy the unified fabric of a state, and the values of nationalism and comity are not welcome, as these polarize a state and give its citizens an advantage which infringes upon the nation as an entity.

Various remedies of providing manpower programs as an alternative means to the local residents and limiting hiring preferences to unemployed persons seem logical. This has to be done and developed, keeping in mind the need to balance the respective state and national interests, and the greater national importance of the commodity.

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<sup>138</sup> *Hicklin v. Orbeck*, 565 P.2d 159, 172–73 n.13 (Alaska 1977) (quoting *Douglas v. Seacoast Prods. Inc.*, 431 U.S. 265 (1977)).





# Bitcoin, the Commerce Clause, and *Bayesian Stare Decisis*

F. E. Guerra-Pujol\*

*In most matters it is more important that the applicable rule of law be settled than that it be settled right.*

—Justice Louis Brandeis<sup>1</sup>

*When the facts change, I change my mind. What do you do, sir?*

—Attributed to John Maynard Keynes<sup>2</sup>

## INTRODUCTION

In *South Dakota v. Wayfair*, the U.S. Supreme Court concluded that a state may compel out-of-state retailers to collect taxes on sales to its residents conducted via the Internet.<sup>3</sup> Yet above and beyond retail sales, *Wayfair* also invites us to consider some novel constitutional questions. Does the Commerce Clause,<sup>4</sup> for example, now authorize state and local governments to tax bitcoin transactions, criminalize the sale or use of sex robots, or ban self-driving cars?<sup>5</sup>

Broadly speaking, bitcoin, sex robots, and self-driving cars are specific examples of new technologies or new applications of existing technology—technologies and applications that were unimaginable when I was in law school<sup>6</sup>—such as blockchains or “distributed ledgers” (bitcoin), virtual reality (sex robots), and artificial

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<sup>1</sup> *Burnet v. Coronado Oil & Gas Co.*, 285 U.S. 393, 406 (1932) (Brandeis, J., dissenting).

<sup>2</sup> See QUOTE INVESTIGATOR, “*When the Facts Change, I Change My Mind. What Do You Do, Sir?*,” <https://quoteinvestigator.com/2011/07/22/keynes-change-mind/> [http://perma.cc/J93G-QPNG].

<sup>3</sup> 138 S. Ct. 2080, 2100 (2018).

<sup>4</sup> U.S. CONST. art. I, § 8, cl. 3.

<sup>5</sup> I have chosen these particular examples because there is no direct federal legislation (as of this writing) in these areas.

<sup>6</sup> For the record, I attended law school in the early 1990s.

intelligence (autonomous vehicles).<sup>7</sup> My thesis is that the development and deployment of these revolutionary Internet technologies and platforms will not only require us to reconsider the regulation of “commerce”; they will also invite us to reconsider the nature of precedent. In particular, why should the past trump change? In this age of technological change, why should *stare decisis* be our default rule? Moreover, because our existing principles of horizontal precedent are indeterminate, I will propose a new theory of horizontal precedent, which I call *Bayesian stare decisis*.<sup>8</sup>

The remainder of this Article is organized as follows: Part I briefly considers the taxation of bitcoin transactions to give the reader some sense of the constitutional Pandora’s box that *Wayfair* just opened. Part II then delves into one aspect of the *Wayfair* decision that has broad implications for the future. Specifically, when does technological change justify a departure from the Court’s previous Commerce Clause decisions? Part III sketches a possible solution to the problem of horizontal precedent. Part IV summarizes my proposal and concludes.

### I. MOTIVATING EXAMPLE: BITCOIN

The development of new Internet applications and technologies, such as bitcoin, sex robots, and self-driving cars, raise deep and difficult questions about the meaning of commerce and the wisdom of the *Wayfair* decision going forward. Given the lack of direct federal legislation in these domains, does the Commerce Clause (as per *Wayfair*) authorize state and local governments to tax bitcoin transactions, criminalize the sale or use of sex robots, or ban self-driving cars?

For purposes of illustration, I will consider the taxation of bitcoin as an exemplar or paradigm case.<sup>9</sup> In particular, given the holding in *Wayfair*, could a state now impose a sales tax on “blockchain” transactions or a property tax on cryptocurrency holdings? The answer to this conjecture will depend on how blockchains or “distributed ledgers” are classified for tax purposes.

Nor is this an idle question. At the federal level, the Internal Revenue Service published a notice providing answers to

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<sup>7</sup> For some recent literature exploring other dimensions of these new technologies, see ROBOT SEX: SOCIAL AND ETHICAL IMPLICATIONS 1 (John Danaher & Neil McArthur eds., 2017); HOD LIPSON & MELBA KURMAN, DRIVERLESS: INTELLIGENT CARS AND THE ROAD AHEAD viii (2018); see also PRIMAVERA DE FILIPPI & AARON WRIGHT, BLOCKCHAIN AND THE LAW: THE RULE OF CODE 3 (2018).

<sup>8</sup> See *infra* Part III.

<sup>9</sup> For an influential treatment of the use of exemplars in the domain of knowledge production, see 2 THOMAS S. KUHN, THE STRUCTURE OF SCIENTIFIC REVOLUTIONS 144–45 (Otto Neurath et al. eds., 2d ed. 1970).

frequently asked questions on virtual currencies like bitcoin.<sup>10</sup> In summary, the position of the IRS is that “[g]eneral tax principles applicable to property transactions apply to transactions using virtual currency.”<sup>11</sup> Cryptocurrencies are thus treated as taxable property, just like shares of stock or physical assets.<sup>12</sup>

At the state level, the regulation of blockchains and cryptocurrencies is, as of this writing (summer of 2018), still an open question. The National Conference of Commissioners on Uniform State Laws approved a “Uniform Regulation of Virtual-Currency Businesses Act” in July 2017.<sup>13</sup> Yet, state laws vary widely as to what goods and services are taxable.<sup>14</sup> As a general rule, however, the sale of most tangible goods is taxable, while the provision of services and other intangibles is usually not taxable.<sup>15</sup> But there are exceptions to the exception. Telecommunications services, for example, are subject to a tax similar to a sales tax in most states.<sup>16</sup>

Returning to my exemplar—the taxation of bitcoin by state and local governments—the answer to my conjecture will depend on how blockchains or “distributed ledgers” are classified for tax purposes. I, however, will leave that transcendental task to tax lawyers and the courts. Instead, I will now ask a deeper question. When should a court cling to its own precedents, and when should it disregard the past? It is this aspect of the *Wayfair* case that motivated me to write this Article.

<sup>10</sup> I.R.S. Notice 2014-21, (Mar. 25, 2014), <https://www.irs.gov/pub/irs-drop/n-14-21.pdf> [<http://perma.cc/8NU9-CDY2>].

<sup>11</sup> *Id.* at 2.

<sup>12</sup> *Id.*

<sup>13</sup> NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, UNIFORM REGULATION OF VIRTUAL CURRENCY BUSINESSES ACT (2017), [http://www.uniformlaws.org/shared/docs/regulation%20of%20virtual%20currencies/2017AM\\_URVCBA\\_AsApproved.pdf](http://www.uniformlaws.org/shared/docs/regulation%20of%20virtual%20currencies/2017AM_URVCBA_AsApproved.pdf) [<http://perma.cc/7DGJ-RL7A>]. Although this model act has been introduced in three states (Connecticut, Hawaii, and Nebraska), as of August 2018 it has not been enacted by a single state. See *Regulation of Virtual-Currency Businesses Act*, UNIFORM LAW COMMISSION, <http://www.uniformlaws.org/Act.aspx?title=Regulation%20of%20VirtualCurrency%20Businesses%20Act> [<http://perma.cc/2E6N-TAPB>].

<sup>14</sup> See generally WALTER HELLERSTEIN ET AL., STATE AND LOCAL TAXATION: CASES AND MATERIALS 841–43 (10th ed. 2014).

<sup>15</sup> See *id.* at 659. As explained by Walter Hellerstein:

If a sale involves a transfer that is limited to tangible personal property (e.g., the typical purchase of goods at a retail store) or a transfer that is limited to services or intangibles (e.g., a haircut or a right to display an image), its taxability under a traditional retail sales tax is not in doubt. The former transaction will be taxable as a sale of tangible personal property; the latter transactions will be exempt as a sale of services or intangibles.

*Id.*

<sup>16</sup> See, e.g., Gregory H. Wassall & John J. Sullivan, *State Taxation of Telecommunications Companies*, 79 PROC. OF THE ANN. CONF. ON TAX’N 342, 342 (1987).

## II. THE PROBLEMS WITH PRECEDENT

What is the primary purpose of precedent? Is it about promoting the rule of law?<sup>17</sup> Is it about the creation of community-wide and intertemporal coherence?<sup>18</sup> The protection of settled expectations and reliance interests?<sup>19</sup> Or the laying down of general rules?<sup>20</sup> In short, legal scholars and judges have articulated a wide variety of justifications for stare decisis. But as I shall argue below, *Wayfair* shows why these justifications are descriptively weak and normatively unpersuasive. Moreover, whatever theory of precedent you subscribe to,<sup>21</sup> stare decisis poses an even deeper puzzle. Why should the past determine the future in the domain of law? After all, it is axiomatic that “one congress cannot bind a future congress” just as the decisions of one president do not bind a future a president.<sup>22</sup> Why should the Judicial Branch be any different?

Stare decisis is an example of *path dependence*, or the idea that the past matters.<sup>23</sup> But from a normative perspective, it is not obvious whether path dependence in law is good or bad on balance. Some say that stare decisis for its own sake is a bad thing, or in the words of then-Judge Benjamin Cardozo, “when a rule, after it has been duly tested by experience, has been found to be inconsistent with the sense of justice or with the social welfare, there should be less hesitation in frank avowal and full abandonment.”<sup>24</sup> Others take a more benign view of path dependence in law. Justice Louis

17 See Jeremy Waldron, *Stare Decisis and the Rule of Law: A Layered Approach*, 111 MICH. L. REV. 1, 1 (2012).

18 See RONALD DWORKIN, LAW'S EMPIRE 225, 227, 243, 251 (1986).

19 See Randy J. Kozel, *Precedent and Reliance*, 62 EMORY L.J. 1459, 1459, 1506 (2013).

20 See FREDERICK SCHAUER, PLAYING BY THE RULES: A PHILOSOPHICAL EXAMINATION OF RULE-BASED DECISION-MAKING IN LAW AND IN LIFE 174–75, 177, 181–82 (1991); see also Grant Lamond, *Precedent and Analogy in Legal Reasoning*, THE STANFORD ENCYCLOPEDIA OF PHILOSOPHY § 2.1 (2016), <https://plato.stanford.edu/archives/spr2016/entries/legal-reas-prec/> [http://perma.cc/TMT5-PSLB]. Cf. Larry Alexander, *Constrained by Precedent*, 63 S. CAL. L. REV. 1, 17–19 (1989) (describing “the rule model of precedent”).

21 See *supra* notes 17–20 and accompanying text.

22 See, e.g., Larry Alexander & Saikrishna Prakash, *Mother May I? Imposing Mandatory Prospective Rules of Statutory Interpretation*, 20 CONST. COMMENT. 97, 98–99 (2003). But see Eric A. Posner & Adrian Vermeule, *Legislative Entrenchment: A Reappraisal*, 111 YALE L.J. 1665, 1666 (2002).

23 See generally S. J. Liebowitz & Stephen E. Margolis, *Path Dependence, Lock-In, and History*, 11 J. L., ECON., & ORG. 205, 205 (1995). Cf. F. E. Guerra-Pujol, *Puerto Rico as a Critical Locality: Is a Post-Colonial Puerto Rico Possible? A Game-Theoretic Analysis of the Impasse Over Puerto Rico's Status*, 20 ST. THOMAS L. REV. 561, 568–69 (2008) (applying the concept of path dependence to the debate over Puerto Rico's constitutional status).

24 BENJAMIN N. CARDOZO, THE NATURE OF THE JUDICIAL PROCESS 150 (1921). For his part, Randy Kozel refers to this feature of stare decisis disparagingly as “unadorned path dependence.” Cf. Randy J. Kozel, *The Rule of Law and the Perils of Precedent*, 111 MICH. L. REV. FIRST IMPRESSIONS 37, 40 (2013) (“There is value in a citizen's power to advocate her interests before governmental bodies and to receive an explanation for defeat that is more satisfying than unadorned path-dependence.”).

Brandeis, for example, famously asserted that “[s]tare decisis is usually the wise policy, because in most matters it is more important that the applicable rule of law be settled than that it be settled right.”<sup>25</sup> Or in the words of Richard Posner, “The reason for path dependence in law is . . . the cost of adapting to a sudden change in law by changing practices adopted in reliance on the law before it changed.”<sup>26</sup>

At the same time, judging is supposed to be a species of critical thinking and practical reason, but to the extent that horizontal precedent privileges the past, stare decisis tends to foreclose the use of reason.<sup>27</sup> But why? Why should law be immune to reason? For as John Maynard Keynes is reported to have said, “When the facts change, I change my mind. What do you do, sir?”<sup>28</sup> In short, how should someone committed to stare decisis respond to Keynes’s query?

#### A. Competing Visions of Stare Decisis in *Wayfair*

In *South Dakota v. Wayfair*,<sup>29</sup> the Court concluded that a state may require an out-of-state seller with no physical presence in the state to collect and remit sales taxes on goods the seller ships to consumers in the state. To reach this result, however, the Court overturned two long-standing Commerce Clause precedents: *National Bellas Hess, Inc. v. Department of Revenue*<sup>30</sup> and *Quill Corp. v. North Dakota*.<sup>31</sup> In reality, direct departures from stare decisis by the Supreme Court are exceedingly rare, for the Court has overturned a previous decision only a handful of

<sup>25</sup> *Burnet v. Coronado Oil & Gas Co.*, 285 U.S. 393, 406 (1932) (Brandeis, J., dissenting).

<sup>26</sup> RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 561 (6th ed. 2003).

<sup>27</sup> *See, e.g.*, RANDY J. KOZEL, *SETTLED VERSUS RIGHT: A THEORY OF PRECEDENT* 50 (2017) (“[T]he deferring judge might find herself compelled to ignore the lessons of experience in order to keep faith with the past.”). *Cf.* NEIL DUXBURY, *THE NATURE AND AUTHORITY OF PRECEDENT* 2–3 (2008) (distinguishing between decision-making based on experience and decision-making based on precedent).

<sup>28</sup> *See, e.g.*, Wei Li, *Changing One’s Mind When the Facts Change: Incentives of Experts and the Design of Reporting Protocols*, 74 *REV. ECON. STUD.* 1175, 1175 (2007); Luigi L. Pasinetti, *The Cambridge School of Keynesian Economics*, 29 *CAMBRIDGE J. ECON.* 837, 841 (2005). As an aside, although this quotation is often attributed to Keynes in the literature, its provenance is contested. The genesis of the structure of this formulation (i.e. “when *x* changes, I change my mind,” where *x* is “the facts” or “information”) may, in fact, be Paul Samuelson, not Keynes. *See* QUOTE INVESTIGATOR, *supra* note 2.

<sup>29</sup> 138 S. Ct. 2080, 2094 (2018).

<sup>30</sup> 386 U.S. 753, 759–60 (1967), *overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<sup>31</sup> 504 U.S. 298, 317 (1992), *overruled by* *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018). *Quill*, decided by a margin of 8 to 1, could be likened to a “super precedent.” *See* Michael J. Gerhardt, *Super Precedent*, 90 *MINN. L. REV.* 1204, 1205 (2006). *See Wayfair* 138 S. Ct. at 2099 (overruling *Quill* and *Bellas Hess*).

times.<sup>32</sup> Nevertheless, although *Wayfair* is the exception to the stare decisis rule, I will focus on a deeper jurisprudential question posed by *Wayfair* in the remainder of this paper: How constraining should stare decisis be? For above and beyond the Court's contested interpretation of the Commerce Clause,<sup>33</sup> *Wayfair* also poses a perennial jurisprudential puzzle: The tension between stability and change. Or to borrow Justice Brandeis's classic formulation of the problem, is it more important for the law to be settled or for the law to be right?<sup>34</sup> In short, what is the probability that *Wayfair* itself will be overturned in some future case, especially in light of the new Internet applications and technologies that we surveyed above?

But before outlining the competing visions of precedent in *Wayfair*, let's restate the facts of the case.<sup>35</sup> In 2016, South Dakota enacted a sales tax law declaring a state of emergency.<sup>36</sup> The bottom line, so to speak, was that South Dakota was not collecting enough tax revenue. The law thus required some out-of-state sellers to collect South Dakota's sales tax on all goods shipped into South Dakota.<sup>37</sup> The problem with the South Dakota statute, however, is that it effectively overruled two previous U.S. Supreme Court cases, *Bellas Hess* and *Quill*.<sup>38</sup> These precedent cases imposed a bright-line limit on the interstate collection of sales taxes: A state may not require an out-of-state seller to collect the state's sales taxes if the business lacks a physical presence in the state.<sup>39</sup> But the problem with this physical presence rule, in turn, is that a state must rely on its

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<sup>32</sup> By way of example, Professor Jonathan Adler recently measured the frequency with which the Supreme Court overturns its prior precedents. According to Professor Adler, in the previous thirteen years (i.e., since John Roberts was appointed Chief Justice of the U.S. Supreme Court), during which the Court has decided close to 1000 cases, it has overruled eighteen of its previous decisions. Jonathan H. Adler, *The Stare Decisis Court?*, VOLOKH CONSPIRACY (July 8, 2018), <https://reason.com/volokh/2018/07/08/the-stare-decisius-court> [<http://perma.cc/B5WT-2MUB>].

<sup>33</sup> Cf. David F. Forte, *Commerce, Commerce, Everywhere: The Uses and Abuses of the Commerce Clause*, HERITAGE FOUND. (Jan. 18, 2011), <https://www.heritage.org/the-constitution/report/commerce-commerce-everywhere-the-uses-and-abuses-the-commerce-clause> [<http://perma.cc/PNU2-24A3>] ("No clause in the 1787 Constitution has been more disputed, and it has generated more cases than any other.")

<sup>34</sup> See *Burnet v. Coronado Oil & Gas Co.*, 285 U.S. 393, 406 (1932) (Brandeis, J., dissenting) ("Stare decisis is usually the wise policy, because in most matters it is more important that the applicable rule of law be settled than that it be settled right.")

<sup>35</sup> If the reader is already familiar with the facts and the main issues in *Wayfair*, feel free to skip this and the following paragraph.

<sup>36</sup> S. 106, 2016 Leg. Assemb., 91st Sess. (S.D. 2016).

<sup>37</sup> *Id.* Despite the South Dakota legislature's self-serving state-of-emergency declaration, the statute exempted out-of-state sellers who deliver less than \$100,000 of goods into the state per annum or who engage in less than 200 separate transactions for the delivery of goods into the state per annum. See *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2089 (2018).

<sup>38</sup> See S. 106, 2016 Leg. Assemb., 91st Sess. (S.D. 2016).

<sup>39</sup> See *Wayfair*, 138 S. Ct. at 2091.



residents to pay the sales tax owed on their purchases from out-of-state sellers, and consumers don't like paying taxes!<sup>40</sup>

A legal duel then ensued when Wayfair, along with two other major online retailers (Overstock and Newegg), decided to challenge the South Dakota statute in court.<sup>41</sup> Since none of these business firms had a physical presence in South Dakota, the lower courts followed precedent and ruled in their favor.<sup>42</sup> So far, so good. But South Dakota officials rolled the dice and appealed all the way up to the U.S. Supreme Court, and their gamble paid off. Five Justices (a bare majority) voted to overrule their Court's previous precedents.<sup>43</sup> Thus, beyond the Commerce Clause question, *Wayfair* poses a deeper question about stare decisis. To be clear, this deeper question was not about the scope of the *Quill* precedent but rather about its strength. Specifically, when is a court justified in overturning its own precedents?

In particular, *Wayfair* poses the problem of *horizontal precedent*, the obligation of a court to follow the decisions by the same court in previous cases.<sup>44</sup> Accordingly, this paper will put aside the practice of *vertical precedent*, or the obligation of a lower court to obey the decisions of a court above it in the judicial hierarchy.<sup>45</sup> It is one thing for a lower court to follow the chain of command, but why should the highest court of a legal jurisdiction, such as the U.S. Supreme Court, be bound by its own previous decisions?

The *Wayfair* Court split 5 to 4 on the question of stare decisis.<sup>46</sup> Consider first the majority opinion by Justice Kennedy. In justifying the Court's decision to depart from stare decisis, the majority opinion emphasizes the changes that have occurred since the precedent cases were decided:

[T]he real world implementation of Commerce Clause doctrines now makes it manifest that the physical presence rule as defined by *Quill* must give way to the "far-reaching systemic and structural changes in the economy" and "many other societal dimensions" caused by the Cyber Age. Though *Quill* was wrong on its own terms when it was

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40 Or in the words of the *Wayfair* court: "consumer compliance rates are notoriously low." *Id.* at 2088 (citing U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-18-114, REPORT TO CONGRESSIONAL REQUESTERS: SALES TAXES, STATES COULD GAIN REVENUE FROM EXPANDED AUTHORITY, BUT BUSINESSES ARE LIKELY TO EXPERIENCE COMPLIANCE COSTS 5 (2017)).

41 *Id.* at 2089.

42 *Id.*

43 *Id.* at 2087.

44 IAN MCLEOD, LEGAL METHOD 153–59 (2d. ed. 1996).

45 *Id.*

46 *Wayfair*, 138 S. Ct. at 2087.

decided in 1992, since then the Internet revolution has made its earlier error all the more egregious and harmful.<sup>47</sup>

In other words, a precedent must give way when the conditions that produced that precedent have changed. When the facts change, so should the law.

By contrast, the dissent emphasizes the disruption and transition costs that will follow from the Court's decision to overturn its precedents:

I agree that *Bellas Hess* was wrongly decided, for many of the reasons given by the Court. The Court argues in favor of overturning that decision because the "Internet's prevalence and power have changed the dynamics of the national economy." But that is the very reason I oppose discarding the physical-presence rule. E-commerce has grown into a significant and vibrant part of our national economy against the backdrop of established rules, including the physical-presence rule. Any alteration to those rules with the potential to disrupt the development of such a critical segment of the economy should be undertaken by Congress. The Court should not act on this important question of current economic policy, solely to expiate a mistake it made over 50 years ago.<sup>48</sup>

Simply put, it is more important that the law be settled than right. Error is costly, but so too is change. *Wayfair* thus presents competing visions of the strength of stare decisis. It is thus the perfect case to test our intuitions and theories of stare decisis.

## B. The Stare Decisis Swamp

*Wayfair* shows there are different ways of drawing the line between stability and change. Many judges, following the lead of Judge Cardozo, would draw the line on pragmatic or consequentialist grounds, or in the eloquent words of Judge Cardozo: "when a rule, after it has been duly tested by experience, has been found to be inconsistent with the sense of justice or with the social welfare, there should be less hesitation in frank avowal and full abandonment."<sup>49</sup>

The problem with such prudential or pragmatic justifications, however, is that there are also many prudential and pragmatic reasons for respecting precedent, even flawed precedent.<sup>50</sup> Judges have identified a plethora of reasons for deferring to a previous decision, even when there is a consensus that the prior case was wrongly decided.<sup>51</sup> These reasons include the promotion of judicial

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<sup>47</sup> *Id.* at 2097 (internal citation omitted).

<sup>48</sup> *Id.* at 2101 (Roberts, C.J., dissenting) (internal citation omitted).

<sup>49</sup> CARDOZO, *supra* note 24, at 150.

<sup>50</sup> *See, e.g.*, KOZEL, *supra* note 27, at 36–42, 46–48.

<sup>51</sup> *Id.* at 36–49.

efficiency, the advancement of collective wisdom, the furtherance of uniformity and common ground, and the protection of reliance interests.<sup>52</sup> Of these justifications for stare decisis, reliance is the most important, so I begin there.

The relationship between precedent and reliance is a close one: Once a court decides a question of law, various actors may take the court's decision into account, modifying their behavior in light of the court's previous decision. It would thus be unfair for a court to upset the settled expectations of parties who have relied on that court's own past decisions to organize their affairs.<sup>53</sup> These reliance interests are especially salient in a commercial context, such as entering into a contract or setting up a business.

Although the protection of reliance interests is one of the most prevalent justifications for deference to precedent,<sup>54</sup> it turns out that this justification is flimsy and unpersuasive. In particular, there are several problems with the reliance argument. One is the problem of multiple stakeholders. Another is that reliance is misplaced when conditions have changed. Yet another is the problem of abusive or unreasonable expectations. I will explore each of these problems below.

The main problem with the reliance theory of precedent is the problem of multiple stakeholders. In brief, any given precedent will have multiple stakeholders, and these various stakeholders may have varying reliance interests and competing expectations about the soundness of a precedent and about the transition costs of overturning a precedent. Furthermore, *Wayfair* itself provides a textbook illustration of these problems with the reliance theory of precedent. In *Wayfair*, the competing stakeholders were the States, who wanted to collect additional tax revenues, and Internet retailers like Wayfair and Overstock, who wanted to avoid the burdens of direct taxation in states where they had no physical presence.<sup>55</sup>

But even if there were a single stakeholder (as opposed to multiple stakeholders), or even if the multiple stakeholders shared the exact same reliance interests, the reliance theory of precedent would still be unsound for two additional reasons. One is the possibility of misplaced reliance. The other is the possibility of abusive or strategic reliance.

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<sup>52</sup> See generally Campbell H. Black, *The Principle of Stare Decisis*, 34 AM. L. REG. (1852–1891) 745 (1886).

<sup>53</sup> See, e.g., *Walter v. Arizona*, 497 U.S. 639, 673, (“The doctrine [of stare decisis] exists for the purpose of introducing certainty and stability into the law and protecting the expectations of individuals and institutions that have acted in reliance on existing rules.”).

<sup>54</sup> Kozel, *supra* note 19, at 1459.

<sup>55</sup> *Wayfair*, 138 S. Ct. at 2089.

Reliance might be “misplaced,” especially when the economic or social conditions on which a previous decision was based have changed, or in the words of Judge Richard Posner, “[w]e would . . . expect, and we find, that stare decisis is less rigidly adhered to the more rapidly the society is changing.”<sup>56</sup> Namely, the possibility of a *Wayfair*-like decision—of a precedent case being overturned due to changing condition—is thus a known risk of litigation. In the words of Judge Cardozo, this is “a fair risk of the game of life, not different in degree from the risk of any other misconception of right or duty.”<sup>57</sup>

That is to say, there are no absolutes in life, even in the domain of precedent. Specifically, even when the Supreme Court is paying lip service to the doctrine of stare decisis, it has consistently stated that all precedents are subject to revision. Since courts have the discretion to overrule their previous decisions, one could argue “reliance on a flawed precedent should be treated as a calculated risk.”<sup>58</sup> On this view, reliance on a court’s decision, knowing full well that precedents can be overturned, is like placing a bet. This probabilistic view of precedent, in turn, poses a new question: How should these probabilities be calculated?

The other reason why reliance is a weak argument is the problem of abusive or unreasonable expectations. Once again, the *Wayfair* case provides a textbook illustration of this problem. Although the Court acknowledges that “[r]eliance interests are a legitimate consideration when the Court weighs adherence to an earlier but flawed precedent,” it also suggests that some of the reliance on *Quill* was improperly motivated.<sup>59</sup> In particular, some Internet retailers were hoping to gain an unfair advantage over firms with a physical presence in a taxing jurisdiction. According to the Court, “[s]ome remote retailers go so far as to advertise sales as tax free.”<sup>60</sup> The Court denigrates the reliance of out-of-state Internet retailers thus: “[A] business ‘is in no position to found a constitutional right . . . on the practical opportunities for tax avoidance.’”<sup>61</sup>

But this line of reasoning in the *Wayfair* Court’s majority opinion poses a new problem: How does one distinguish between legitimate expectations (those that deserve to be protected) and undeserving or unscrupulous ones? What if only “some” parties

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<sup>56</sup> POSNER, *supra* note 26, at 560.

<sup>57</sup> CARDOZO, *supra* note 24, at 148.

<sup>58</sup> KOZEL, *supra* note 27, at 48.

<sup>59</sup> South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2098 (2018).

<sup>60</sup> *Id.*

<sup>61</sup> *Id.* at 2086 (quoting Nelson v. Sears, Roebuck & Co., 312 U.S. 359, 366 (1941)).

have such unreasonable expectations? Where should a court draw the line?

Aside from reliance, another justification for stare decisis is that it promotes the “rule of law.”<sup>62</sup> But as Professor Randy Kozel has shown, this justification is far from obvious, since the “rule-of-law benefits of stare decisis are invariably accompanied by rule-of-law costs.”<sup>63</sup> One could even argue that the doctrine of stare decisis does more harm than good to the rule of law.<sup>64</sup> How does stare decisis harm the rule of law? By privileging stability over accuracy and thus obstructing the use of reason. Judges who follow precedent don’t ask, *what is the best way of deciding this case?* Instead, stare decisis requires judges to ask a different question: *Have we decided this question before?* But there is no necessary logical relation between the timing of a decision and its accuracy.<sup>65</sup> In short, the doctrine of stare decisis not only makes it more difficult to overturn a flawed precedent; it also hinders the use of reason.

For its part, *Wayfair* is a textbook illustration of this anti-stare-decisis argument: “If it becomes apparent that the Court’s Commerce Clause decisions prohibit the States from exercising their lawful sovereign powers in our federal system, the Court should be vigilant in correcting the error.”<sup>66</sup> In other words, courts should fix their mistakes instead of abiding by and perpetuating them, especially in cases involving constitutional interpretation. Or in the words of the late Justice Antonin Scalia, “[t]he whole function of [stare decisis] is to make us say that what is false under proper analysis must nonetheless be held to be true . . . .”<sup>67</sup> According to Justice Scalia, his oath as a Justice was to support and defend the Constitution, not to support and defend his predecessors’ interpretations of the Constitution.<sup>68</sup>

Another justification for stare decisis is predictability or stability. Even a champion of the pragmatic view like Judge Cardozo concedes “[t]he situation would . . . be intolerable if the weekly changes in the composition of the court were accompanied

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<sup>62</sup> See Waldron, *supra* note 17, at 3–4. As an aside, “rule of law” can mean different things to different people. By “rule of law,” I mean the idea that every person—including lawmakers and judges—must obey the law.

<sup>63</sup> Kozel, *supra* note 24, at 38.

<sup>64</sup> *Id.* at 41 (“Deferring to precedent can generate rule-of-law costs that may offset the countervailing benefits.”).

<sup>65</sup> See, e.g., Arbora Resulaj et al., *Changes of Mind in Decision-Making*, 461 NATURE 263, 263 (2009).

<sup>66</sup> *Wayfair*, 138 S. Ct. at 2096.

<sup>67</sup> See ANTONIN SCALIA, A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW 139 (Amy Gutmann ed., 1997).

<sup>68</sup> See *id.*

by changes in its rulings.”<sup>69</sup> By way of example, *Quill* was decided by a vote of 8 to 1, while *Wayfair* was decided by a 5 to 4 vote. But at the same time, only two Justices who participated in the precedent case (*Quill*) also took part in the subsequent case (*Wayfair*).<sup>70</sup> Although a generational span of over twenty-five years separates both decisions, one is tempted to believe that the replacement of the other seven Justices with new ones during this span of time played a significant role in the outcome of the subsequent case.<sup>71</sup>

Yet another justification for the rule of stare decisis is *judicial efficiency*. Even a pragmatist like Judge Cardozo concedes: “the labor of judges would be increased almost to the breaking point if every past decision could be reopened in every case . . . .”<sup>72</sup> This concern (judicial efficiency) is especially salient in Commerce Clause cases, since most legislation has some connection, however tenuous, to commerce and since so much local legislation is protectionist in nature.<sup>73</sup> If ever there were an area of law where stability mattered more than getting it right, it would be the Commerce Clause. But why should efficiency trump accuracy?

In short, the arguments in favor of precedent turn out to be rather flimsy and unpersuasive. In truth, stare decisis is an indeterminate doctrine.

### C. The Bottom Line: Horizontal Precedent is Indeterminate

Stare decisis is an indeterminate doctrine because it is easy to find a reason for overruling a previous precedent when the precedent case is wrong. True, when a previous case is deemed to be wrongly decided, judges are supposed to apply precedent unless there is a good reason or special justification for overruling it.<sup>74</sup> But the problem with this test is that it is not very demanding.

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<sup>69</sup> CARDOZO, *supra* note 24, at 150.

<sup>70</sup> Anthony Kennedy and Clarence Thomas were the only Justices who participated in both decisions. See *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992); *Wayfair*, 138 S. Ct. at 2080.

<sup>71</sup> The careful reader will notice that I hedged my previous statement with the words “tempted to believe.” I did this because, in fact, both Justice Kennedy and Justice Thomas changed their minds regarding the correctness of *Quill* and ended up voting to overturn their Court’s own precedent. That is, they both thought in good faith that the error in *Quill* was sufficiently egregious to justify overturning it. Cf. CARDOZO, *supra* note 24, at 158 (“The United States Supreme Court and the highest courts of the several states overrule their own prior decisions when manifestly erroneous.”).

<sup>72</sup> CARDOZO, *supra* note 24, at 149.

<sup>73</sup> See, e.g., Wendy E. Takacs, *Pressures for Protectionism: An Empirical Analysis* 19 ECON. INQUIRY 687, 691–92 (1981).

<sup>74</sup> Cf. *Planned Parenthood of Se. Pa. v. Casey*, 505 U.S. 833, 864 (1992) (“[A] decision to overrule should rest on some special reason over and above the belief that a prior case was wrongly decided.”).



How hard can it be for a creative or motivated judge to find a “special reason” when he needs one? *Wayfair* itself is a textbook illustration of this problem.

In *Wayfair* that “special reason” was the unfairness of the physical presence rule. Specifically, the Court claims that the physical presence rule creates an “unfair and unjust” tax loophole:

The [physical presence rule] is unfair and unjust to those competitors, both local and out of State, who must remit the tax; to the consumers who pay the tax; and to the States that seek fair enforcement of the sales tax, a tax many States for many years have considered an indispensable source for raising revenue.<sup>75</sup>

The Court also goes on to say that “there is nothing unfair about requiring companies that avail themselves of the States’ benefits to bear an equal share of the burden of tax collection.”<sup>76</sup>

In other words, the physical presence rule harms two different groups of people. Since this rule makes it more difficult for states to collect sales taxes from out-of-state sellers with no physical presence in their state, it harms tax collectors in remote places like South Dakota. And it also harms business firms who do happen to have a physical presence in South Dakota, since they must collect and remit sales taxes on their in-state sales, while their competitors (the ones with no physical presence in South Dakota) do not.

For my part, I do not dispute that the physical presence rule is unfair, since it creates serious harms and economic distortions.<sup>77</sup> The problem with this argument, however, is that getting rid of the physical presence rule is also unfair and will likewise produce serious harms and distortions.<sup>78</sup> In short, by overturning its pro-physical-presence precedents, the Court’s decision will harm consumers as well as out-of-state sellers, or in the words of Chief Justice Roberts’ dissenting opinion: “[T]he marketplace itself could be affected by abandoning the physical-presence rule. The [majority’s] focus on unfairness and injustice does not appear to embrace consideration of that current public policy concern.”<sup>79</sup>

<sup>75</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2096 (2018).

<sup>76</sup> *Id.*

<sup>77</sup> See, e.g., Sarah Horn et al., *Supreme Court Abandons Physical Presence Standard: An In-Depth Look at South Dakota v. Wayfair*, THOMSON REUTERS (June 22, 2018), <https://tax.thomsonreuters.com/news/supreme-court-abandons-physical-presence-standard-an-in-depth-look-at-south-dakota-v-wayfair> [<http://perma.cc/47F8-NGZP>] (“[T]he physical presence rule . . . has created unfair and unjust marketplace distortions favoring remote sellers and causing states to lose out on enormous amounts of tax revenue.”).

<sup>78</sup> See, e.g., Steven Malanga, *Why Wayfair Isn’t Fair*, C. J. (June 26, 2018), <https://www.city-journal.org/html/why-wayfair-isnt-fair-15990.html> [<http://perma.cc/HCW5-UKTA>].

<sup>79</sup> *Wayfair*, 138 S. Ct. at 2103 (Roberts, C.J., dissenting).

In short, the problem is not whether *x* rule or *y* loophole is unfair; the problem is figuring out which rule is less unfair.

But there is an additional (and even more important) consideration at play in the *Wayfair* case: stare decisis. In other words, since the Supreme Court had already established the bright-line physical presence rule in previous cases, there is an additional harm we must take into consideration—the macro or system-wide harms to the rule of law and to the values of stability and predictability. The problem with this pro-stare decisis argument, however, is that these justifications for stare decisis are contested and open to debate. After all, if the correction of error and the use of reason should trump the past, why pretend that precedents matter? Why perpetuate the fiction of stare decisis? *Wayfair* thus poses a deeper puzzle: Where should the Justices draw the line between stability (the need to respect precedent) and change (the need to abandon flawed precedents or correct errors)?

To sum up, stare decisis is an indeterminate doctrine. It will always be possible to find or manufacture a good reason for overturning a precedent case, and it will always be possible to rebut such a reason. But it takes a theory to beat a theory.<sup>80</sup> I will thus present a brief and tentative sketch of a Bayesian theory of stare decisis below. In summary, instead of attempting to solve an intractable problem—the inherent tension between stability and change—my Bayesian approach brings stare decisis' indeterminacy out in the open.

### III. SKETCH OF A POSSIBLE SOLUTION: BAYESIAN VOTING<sup>81</sup>

The ultimate problem with precedent is due less to the line-drawing challenges described above<sup>82</sup> and more to the system of majority voting that courts like the U.S. Supreme Court use to decide cases. The problems with majority voting have been noted by others.<sup>83</sup> In brief, majority voting system can be gamed via agenda setting and strategic voting.<sup>84</sup> In the context of horizontal stare decisis, the problem with majority voting is

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<sup>80</sup> For the origins of this oft-quoted maxim (“it takes a theory to beat a theory”), see Larry Solum, *Legal Theory Lexicon: It Takes a Theory to Beat a Theory*, LEGAL THEORY BLOG (Oct. 21, 2012), <http://lsolum.typepad.com/legaltheory/2012/10/introduction-it-takes-a-theory-to-beat-a-theory-this-is-surely-one-of-the-top-ten-all-time-comments-uttered-by-law-professo.html> [<http://perma.cc/QT2D-34YL>].

<sup>81</sup> For an explanation of Bayes' theorem on which this model is based, see Joseph Berkson, *Bayes' Theorem*, 1 ANNALS MATHEMATICAL STAT. 42 (1930).

<sup>82</sup> See Part II, *supra*.

<sup>83</sup> See, e.g., Frank H. Easterbrook, *Ways of Criticizing the Court*, 95 HARV. L. REV. 802, 802 (1982).

<sup>84</sup> *Id.* at 817–23.

that each judge must emit a binary vote to either affirm the precedent case or overturn it. But in truth, the problem of precedent is a matter of degree.

I thus propose a new approach to horizontal precedent: *Bayesian stare decisis*. That is, instead of asking judges to draw an impossible line between stability and change, why not ask them to use some alternative voting procedure, one that requires them to candidly disclose their subjective views regarding the strength of a contested precedent. Specifically, I would ask the Justices to consider adopting the following “Bayesian voting” procedure in which they would openly disclose their subjective evaluations of a precedent’s vitality by ranking its strength on some fixed scale, such as the  $[0, 1]$  interval.<sup>85</sup>

The type of Bayesian voting I am proposing here is often called “range voting” or “utilitarian voting” in the literature on voting systems.<sup>86</sup> I shall call this alternative procedure “Bayesian voting,”<sup>87</sup> or in the context of horizontal precedent, *Bayesian stare decisis*. The virtue of this approach is that it candidly acknowledges the inherently subjective nature of the choice between stability and change.

In summary, in cases in which the Supreme Court is considering whether to overturn one of its previous decisions, each Justice would assign a numerical score reflecting the strength of the precedent case. To be more precise, this score would reflect the Justice’s subjective belief in the precedent’s strength. To keep things simple, this degree of belief could be expressed in numerical terms anywhere in the range from 0 to 1, or 1 to 10, or some other uniform scale. The higher the score, the greater the Justice’s degree of belief in the strength of the precedent case. Let’s use the 0 to 1 scale to illustrate this idea. A score above 0.5 would indicate that the precedent is a strong one and should not be

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<sup>85</sup> In theory, this Bayesian voting procedure could be applied to questions of precedential *scope* and to questions of precedential *strength*. That is, a judge could just as well use this Bayesian voting procedure to rank a precedent’s strength, i.e., whether a previous case should be overturned or not, or its scope, i.e., whether statement *x* is the holding or dicta. Here, however, I will limit my proposal to the question of strength, i.e., to cases in which the Court is considering overturning a precedent case.

<sup>86</sup> See generally Warren D. Smith, Range Voting (Nov. 28, 2000) (unpublished manuscript), <http://citeseerx.ist.psu.edu/viewdoc/download?jsessionid=8F0854766344036D6E9D15E424CFA070?doi=10.1.1.32.9150&rep=rep1&type=pdf> [<http://perma.cc/4TEF-MK9F>]; see also Claude Hillinger, *The Case for Utilitarian Voting*, 22 HOMO Oeconomicus [ECON. MAN] 295, 295 (2005). For a glossary of different voting procedures, see WILLIAM POUNDSTONE, GAMING THE VOTE: WHY ELECTIONS AREN’T FAIR (AND WHAT WE CAN DO ABOUT IT) 287–89 (2008).

<sup>87</sup> See F. E. Guerra-Pujol, *The Case for Bayesian Voting: A Response to Posner and Vermeule* (Jan. 8, 2018) (unpublished manuscript), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3096881](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3096881) [<http://perma.cc/B3ZS-3337>].

overturned, while a score below 0.5 means that the precedent is weak and should be overturned. (A score of 0.5 would mean the judge is undecided about the precedent's precedential strength.)

Under this alternative system of *Bayesian stare decisis*, a precedent would be affirmed if the sum of the Justices' individual scores divided by the number of Justices exceeded some threshold value, say 0.5 if the 0 to 1 scale were used. By contrast, a precedent would be overturned only if the sum of their individual scores divided by the number of Justices voting went below 0.5. (In the event the sum of the Justices' individual scores divided by the number of Justices were exactly 0.5, the Court could require a rehearing of the case.)

My Bayesian approach to precedent recognizes that the strength or scope of a precedent is always a matter of degree, not a binary or all-or-nothing question, or in the words of then-Judge Cardozo, "the duty of a judge [to follow precedent] becomes itself a question of degree . . . ."<sup>88</sup>

Of course, *Bayesian stare decisis* is open to a number of practical objections.<sup>89</sup> Namely, why would the Justices themselves ever agree to implement such an unorthodox voting procedure? That said, my immediate purpose here is not to change the procedures of appellate practice and judging in the short term. My purpose is simply to question the traditional nature of judicial voting (majority rule) and demonstrate the subjective nature of *stare decisis* in close cases.<sup>90</sup>

Moreover, Bayesian voting is not so unorthodox. It is a voting procedure that is commonly used to aggregate collective preferences in many areas of daily life.<sup>91</sup> For instance, "YouTube and Amazon allow users to rate videos and books on a five-point scale. The Internet Movie Database (IMDb) has ten-point ratings of movies."<sup>92</sup> If ordinary people are so accustomed to Bayesian voting in their everyday activities, such as rating movies and restaurants, then my proposed voting procedure should be simple and intuitive enough for the Justices of the Supreme Court.

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<sup>88</sup> CARDOZO, *supra* note 24, at 161.

<sup>89</sup> See Guerra-Pujol, *supra* note 87, at 4. Due to a page-limit constraint, however, I will not rehearse these arguments in this Article.

<sup>90</sup> I have painted my alternative approach to precedent with a broad brush, since this symposium is about the Commerce Clause. Nevertheless, I delve into the details of Bayesian voting and the possibility of Bayesian verdicts in jury trials in my previous work. See *id.*; see also generally F. E. Guerra-Pujol, *Why Don't Juries Try Range Voting*, 51 CRIM. L. BULL. 68 (2015).

<sup>91</sup> See POUNDSTONE, *supra* note 86, at 233.

<sup>92</sup> *Id.*; see also Claude Hillinger, *Science and Ideology in Economic, Political and Social Thought* (Nov. 2006) (unpublished manuscript), [ssrn.com/abstract=945947](http://ssrn.com/abstract=945947) [<http://perma.cc/6HMN-QVJA>].

Before concluding, it is also worth noting that range voting works best when the same group of people rates all the candidates or products.<sup>93</sup> Bayesian voting is thus an especially appropriate method for the Justices, since the same group of people (the Justices) would be rating the strength of a contested precedent. Lastly, in addition to its simplicity and user-friendly nature, Bayesian voting methods are difficult to game via strategic voting. By contrast, when the decisions of the Supreme Court are based on majority rule, stare decisis will remain open to strategic voting.<sup>94</sup>

But the chief virtue of my proposed method of *Bayesian stare decisis* is this: It candidly acknowledges the inherently indeterminate and subjective nature of the choice between stability and change. That is, given the indeterminate nature of precedent, why don't we take an openly probabilistic view of precedent? As the *Wayfair* case itself shows, there is always some positive probability that a previous decision might be overturned, or in the words of the great jurist Oliver Wendell Holmes, "[t]he prophecies of what the courts will do in fact, and nothing more pretentious, are what I mean by the law."<sup>95</sup>

#### IV. CONCLUSION

On a previous occasion, I explored the self-referential nature of stare decisis.<sup>96</sup> When a court embraces the doctrine of stare decisis as an internal rule of procedure, the court's acceptance of stare decisis becomes a precedent. Thus, the doctrine of stare decisis, like any other precedent, can itself be overturned. Nevertheless, it is highly unlikely that the Supreme Court will abandon this doctrine anytime soon. Like the power of judicial review<sup>97</sup> or the landmark decision in *Brown v. Board of Education*,<sup>98</sup> the doctrine of stare decisis has been proclaimed on so many occasions that this doctrine operates as a super precedent, i.e., it has generated so much reliance

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<sup>93</sup> See POUNDSTONE, *supra* note 86, at 233.

<sup>94</sup> See Michael L. Eber, *When the Dissent Creates the Law: Cross-Cutting Majorities and the Prediction Model of Precedent*, 58 EMORY L.J. 207, 207 (2008).

<sup>95</sup> Oliver Wendell Holmes, Jr., *The Path of the Law*, 10 HARV. L. REV. 457, 461 (1897).

<sup>96</sup> See generally F. E. Guerra-Pujol, *Is Stare Decisis a Sand Castle?: An Open Letter to my Law Professor Colleagues*, ARIZ. ST. L.J., (online ed. Oct. 1, 2012), <http://arizonastatelawjournal.org/2012/10/01/is-stare-decisis-a-sand-castle-an-open-letter-to-my-law-professor-colleagues/> [<http://perma.cc/C68J-QFTZ>]. Cf. KOZEL, *supra* note 27, at 172 ("Should the Court give presumptive deference to its precedent about precedent, such that any revisions to the doctrine of stare decisis must be supported by a special justification above and beyond disagreement with the doctrine on the merits?"). A decision overturning stare decisis, however, would produce an even deeper puzzle: Would such a decision be binding in a future case?

<sup>97</sup> See *Marbury v. Madison*, 5 U.S. 137 (1803).

<sup>98</sup> *Brown v. Bd. of Educ.*, 347 U.S. 483 (1954).

and has become so well accepted as to be “practically immune to reconsideration and reversal.”<sup>99</sup>

But that said, the development of new Internet applications and technologies—not only bitcoin but also sex robots, self-driving cars, and so forth—raises deep and difficult questions about the meaning of commerce and the wisdom of the *Wayfair* decision. Because these new technologies and applications are still evolving and their future impact unclear, it would be pure speculation on my part to predict how future courts will apply the *Wayfair* precedent to these new technologies and applications going forward. Instead, I have delved into a deeper problem in this Article—the intractable tension between stability and change—and I have provided a short sketch of a possible solution to this problem: *Bayesian stare decisis* in place of simple majority voting. My approach has the virtue of making the subjective nature of stare decisis open and transparent. Yet, whatever theory of horizontal precedent one prefers, the central normative or prescriptive question remains the same: How constraining should stare decisis be? This question is all the more relevant in light of new Internet applications and technologies.

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<sup>99</sup> Gerhardt, *supra* note 31, at 1206.



# Missouri and Indiana Lay an Egg: Why the Latest Attempt at Invalidating State Factory Farm Regulations Must Fail

*Louis Cholden-Brown\**

At the end of 2017, two original jurisdiction cases addressing the authority of states to regulate the treatment of farm animals were filed at the Supreme Court.<sup>1</sup> Overlapping, but not identical, groups of thirteen States challenged California and Massachusetts laws banning the sale of eggs, as well as pork and veal in Massachusetts, raised in conditions deemed cruel by the defendant States as violative of the Commerce Clause.

These dual challenges, which raise unique questions of original jurisdiction and standing with which this Article does not concern itself, are but the latest in a series of cases seeking to restrict state and local regulation of animal welfare.<sup>2</sup> As with prior attempts, the litigants misconstrue the current thrust of dormant Commerce Clause jurisprudence and the legitimacy of state action to limit its complicity in the spread of disease and moral degradation. Contrary to their invitation, given the broad ambit of the police power and the ill-suitedness of the judiciary to weigh competing local interests and out-of-state burdens, in the absence of discriminatory intent, existing regulatory conflict or inescapable effects on prices or practices, the Court is compelled to uphold such statutes.

This Article begins in Part I by addressing the current conception of the dormant Commerce Clause and its retrenchment, before discussing prior federal litigation concerning subnational laws governing animal food products deemed cruel locally and their

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\* Senior Advisor, New York City 2019 Charter Revision Commission. I am indebted to the many colleagues who first alerted me to these statutes and collaborated in the early phases of the research that became this Article as well as my vegetarian family who were a constant source of support despite never understanding why I was writing about “meat.” The views expressed represent mine alone and are not attributable to any institution or organization with which I am previously or presently affiliated.

<sup>1</sup> Motion For Leave To File Bill Of Complaint, *Missouri v. California*, No. 22O148 (U.S. Dec. 4, 2017); Motion For Leave To File A Bill Of Complaint, *Indiana v. Massachusetts*, No. 22O149 (U.S. Dec. 11, 2017).

<sup>2</sup> See Ernesto Hernández-López, *Sustainable Food and the Constitution*, 50 ARIZ. ST. L.J. 549, 550 (2018).

universal finding of no dormant Commerce Clause conflict in Part II. Parts III and IV in turn chart the passage of the California and Massachusetts statutes respectively, as well as the dormant Commerce Clause arguments presently before the Court. Part V briefly reflects upon the argument advanced by the federal government in response to Calls for the Views of the Solicitor General (CSVGs) in the two cases. Part VI closes by implicating why, when faced with nondiscriminatory laws such as these predicated on legitimate, albeit unquantifiable, local interests, the Court should decline to engage in benefits balancing and uphold the ordinances as rationally related to territorial interests.

### I. DORMANT ELEMENTS OF THE DORMANT COMMERCE CLAUSE

The Commerce Clause authorizes Congress “[t]o regulate Commerce with foreign Nations, and among the several States . . . .”<sup>3</sup> In addition, courts have “long interpreted the Commerce Clause as an implicit restraint on state authority, even in the absence of a conflicting federal statute.”<sup>4</sup> This implicit restraint is often referred to as the dormant, or negative, Commerce Clause.<sup>5</sup> The “fundamental objective” of the dormant Commerce Clause is to protect the national market from “preferential advantages conferred by a State upon its residents or resident competitors.”<sup>6</sup> Therefore, a statute “*motivated* by simple economic protectionism” that “discriminates *on its face* against interstate commerce” is “subject to a virtually *per se* rule of invalidity which can only be overcome by a showing that the State has no other means to advance a legitimate local purpose.”<sup>7</sup> In this dormant Commerce Clause context, discrimination “simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.”<sup>8</sup> However, the Supreme Court “never has articulated clear criteria for deciding when proof of a discriminatory purpose and/or effect is sufficient

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<sup>3</sup> U.S. CONST. art. I, § 8, cl. 3.

<sup>4</sup> *United Haulers Ass’n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 338 (2007) (internal citation omitted).

<sup>5</sup> *General Motors Corp. v. Tracy*, 519 U.S. 278, 287 (1997).

<sup>6</sup> *Brown & Williamson Tobacco Corp. v. Pataki*, 320 F.3d 200, 208 (2d Cir. 2003) (quoting *Tracy*, 519 U.S. at 299) (internal quotation omitted).

<sup>7</sup> *United Haulers Ass’n*, 550 U.S. at 338–39 (emphasis added) (internal citations and quotation omitted). This *per se* rule is motivated by a belief that “when ‘the burden of state regulation falls on interests outside the state, it is unlikely to be alleviated by the operation of those political restraints normally exerted when interests within the state are affected.’” *Id.* at 345 (quoting *S. Pac. Co. v. Ariz. ex rel. Sullivan*, 325 U.S. 761, 767–68 n.2 (1945)). The “abstract possibility” of the existence of less discriminatory means is insufficient to render a statute unconstitutional as the state “is not required to develop new and unproven means of protection . . . .” *Maine v. Taylor*, 477 U.S. 131, 147 (1986) (internal citations and quotation omitted).

<sup>8</sup> *Or. Waste Sys. v. Dep’t of Env’tl. Quality*, 511 U.S. 93, 99 (1994).

for a state or local law to be discriminatory.”<sup>9</sup> “Indeed, the cases in this area seem quite inconsistent”<sup>10</sup> and Justice Scalia has observed “once one gets beyond facial discrimination our negative-Commerce-Clause jurisprudence becomes (and long has been) a quagmire.”<sup>11</sup> The Supreme Court has considered and rejected the argument that a “statute is discriminatory because it will apply most often to out-of-state entities” in a market comprised of more out-of-state than in-state participants.<sup>12</sup> As early as thirty years ago, some argued a “court should strike down a state law if and only if it finds by a preponderance of the evidence that protectionist purpose on the part of the legislators contributed substantially to the adoption of the law or any feature of the law,”<sup>13</sup> and in recent years, the “zone of presumptive illegality”<sup>14</sup> has narrowed to only preclude intentional protectionism.<sup>15</sup>

<sup>9</sup> ERWIN CHERMERINSKY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES 444–45 (4th ed. 2011).

<sup>10</sup> *Id.* at 445.

<sup>11</sup> *W. Lynn Creamery v. Healy*, 512 U.S. 186, 210 (1994) (Scalia, J., concurring) (internal quotation omitted). Justice Scalia was a prolific critic of the dormant Commerce Clause at large. *See, e.g.*, *Comptroller of Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1808 (2015) (Scalia, J., dissenting) (“The fundamental problem with our negative Commerce Clause cases is that the Constitution does not contain a negative Commerce Clause.”). As are Justices Thomas and Gorsuch. *See, e.g.*, *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 614–17 (1997) (Thomas, J., dissenting); *see also* *Direct Mktg. Ass’n v. Brohl*, 814 F.3d 1129, 1148 (10th Cir. 2016) (Gorsuch, J., concurring) (“[T]he whole field in which we are asked to operate today—dormant [C]ommerce [C]lausa doctrine—might be said to be an artifact of judicial precedent.”).

<sup>12</sup> *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 88 (1987).

<sup>13</sup> Donald H. Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091, 1148 (1986).

<sup>14</sup> Daniel Francis, *The Decline of the Dormant Commerce Clause*, 94 DENV. L. REV. 255, 277 (2017).

<sup>15</sup> *See, e.g.*, *C & A Carbone v. Town of Clarkstown*, 511 U.S. 383, 390 (1994) (“The central rationale for the rule against discrimination is to prohibit state or municipal laws whose object is local economic protectionism” because these are the “laws that would excite those jealousies and retaliatory measures the Constitution was designed to prevent”); *United Haulers Ass’n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 338 (2007) (“Discriminatory laws motivated by ‘simple economic protectionism’ are subject to a ‘virtually *per se* rule of invalidity . . . .” (quoting *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978))). It should be noted that arguably *City of Philadelphia* stands for a different principle. *See City of Philadelphia*, 437 U.S. at 624 (“[W]here simple economic protectionism is *effected* by state legislation, a virtually *per se* rule of invalidity has been erected.”) (emphasis added); *see also* *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 273 (1988) (holding that the dormant Commerce Clause “prohibits economic protectionism—that is, regulatory measures *designed to benefit* in-state economic interests by burdening out-of-state competitors”) (emphasis added); *Dep’t of Revenue of Ky. v. Davis*, 553 U.S. 328, 337–38 (2008) (plurality opinion) (“The modern law of what has come to be called the dormant Commerce Clause is driven by concern about ‘economic protectionism that is, regulatory measures *designed to benefit* in-state economic interests by burdening out-of-state competitors.’”) (emphasis added) (internal citation omitted).

By contrast, in what has become known as the *Pike*<sup>16</sup> balancing test, when a statute “regulates even-handedly to effectuate a legitimate local public interest” with only incidental effects on interstate commerce, “it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits.”<sup>17</sup> A putative benefit need not be explicitly stated in the challenged legislation to be legitimate,<sup>18</sup> and neither its wisdom nor effectiveness, nor whether the benefits “actually come into being” are of any consideration.<sup>19</sup>

Absent “discriminating against articles of commerce coming from outside the State,” “the States retain authority under their general police powers to regulate matters of ‘legitimate local concern,’ even though interstate commerce may be affected.”<sup>20</sup> States possess a “right to impose even burdensome regulations in the interest of local health and safety” so long as the regulations are not attempts to “advance their own commercial interests.”<sup>21</sup> The authority to regulate for the public health, safety, morals or welfare is broad,<sup>22</sup> and the power “to prescribe regulations which shall prevent the production within its borders of impure foods” is well established.<sup>23</sup> “[A]rticles as would spread disease and pestilence” are not within the protection of the Commerce Clause regardless of such regulations incidentally affecting interstate commerce, “when the object of the regulation is not to that end, but is a legitimate attempt to protect the people of the state.”<sup>24</sup> The welfare of all animals, not merely those bound for consumption,

16 *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

17 *Id.*

18 *Dean Milk Co. v. City of Madison*, 340 U.S. 348, 354 (1951).

19 *Pharm. Care Mgmt. Ass'n v. Rowe*, 429 F.3d 294, 313 (1st Cir. 2005).

20 *Lewis v. BT Inv. Managers*, 447 U.S. 27, 36 (1980) (internal citation omitted).

21 *H. P. Hood & Sons v. Du Mond*, 336 U.S. 525, 535 (1949).

22 *See, e.g.*, ILL. CONST. art. VII, § 6(a) (West, Westlaw through Sept. 2018) (granting cities in Illinois “the power to regulate for the protection of the public health, safety, morals and welfare”); TUCSON CODE ch. VII § 1(32) (Supp. 2016) (granting mayor and council authority to “adopt and enforce by ordinance all such measures . . . expedient or necessary for the promotion and protection of the health, comfort, safety, life, welfare and property of the inhabitants of the city, the preservation of peace and good order, the promotion of public morals”); *see also* *Mugler v. Kansas*, 123 U.S. 623, 661 (1887) (“It belongs to that department to exert what are known as the police powers of the state, and to determine, primarily, what measures are appropriate or needful for the protection of the public morals, the public health, or the public safety.”); *Cresenzi Bird Imps. v. New York*, 658 F. Supp. 1441, 1447 (S.D.N.Y. 1987) (recognizing the state’s “interest in cleansing its markets of commerce which the Legislature finds to be unethical”); Robert J. Delahunty & Antonio F. Perez, *Moral Communities or a Market State: The Supreme Court’s Vision of the Police Power in the Age of Globalization*, 42 HOUS. L. REV. 637, 676 (2005) (“The States’ authority to pursue specifically moral objectives is deeply rooted in the American constitutional tradition. Indeed, it is one of the fundamental features of our federalism.”).

23 *Sligh v. Kirkwood*, 237 U.S. 52, 59 (1915).

24 *Id.* at 59–60.

is commonly understood to be within that power<sup>25</sup> and, in one series of examples, federal courts have uniformly found the regulation of animal welfare standards for animals for sale as pets do not conflict with the dormant Commerce Clause.<sup>26</sup>

Despite its name, “incidental burdens” are any “burdens on interstate commerce that exceed the burdens on intrastate commerce.”<sup>27</sup> The Commerce Clause “protects the interstate market, not particular interstate firms”<sup>28</sup> and individual losses or businesses restructuring suffered by particular firms do not constitute sufficient burden. Stated otherwise, “the statute, at a minimum, must impose a burden on interstate commerce that is qualitatively or quantitatively different from that imposed on

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<sup>25</sup> See 3B C.J.S. *Animals* § 198 (2018) (“Statutory provisions prohibiting cruelty to animals are sustainable as a valid exercise of the police power.”) (footnote omitted); *Cavel Int’l v. Madigan*, 500 F.3d 551, 557 (7th Cir. 2007) (holding that “[s]tates have a legitimate interest in prolonging the lives of animals that their population happens to like” and that “a state is permitted, within reason, to express disgust at what people do with the dead”); *DeHart v. Town of Austin*, 39 F.3d 718, 722 (7th Cir. 1994) (“The regulation of animals has long been recognized as part of the historic police power of the States.”); *Planned Parenthood of Ind. & Ky. v. Comm’r of Ind. State Dep’t of Health*, No. 17-3163, 2018 WL 3655854, at \*5 (7th Cir. June 25, 2018) (Easterbrook, J., dissenting) (“[A]nimal welfare affects human welfare. Many people feel disgust, humiliation, or shame when animals or their remains are poorly treated.”).

<sup>26</sup> *Park Pet Shop v. City of Chicago*, 872 F.3d 495, 504 (7th Cir. 2017); *N.Y. Pet Welfare Ass’n v. City of New York*, 850 F.3d 79, 92 (2d Cir. 2017) (“[T]here is no need to consider the . . . *Pike* balancing test. Because the Sourcing Law imposes no incidental burdens on interstate commerce, it cannot impose any that are clearly excessive in relation to its local benefits, and therefore survives scrutiny under the dormant Commerce Clause.”); *Mo. Pet Breeders Ass’n v. County of Cook*, 119 F. Supp. 3d 865, 875–76 (N.D. Ill. 2015); *Puppies ’N Love v. City of Phoenix*, 116 F. Supp. 3d 971, 996 (D. Ariz. 2015) (“The Ordinance is not an act of economic protectionism. It is a legitimate attempt to curb the problems associated with the inhumane treatment of animals and local dog homelessness and euthanasia. Plaintiffs’ claim that the Ordinance violates the dormant Commerce Clause fails as a matter of law.”); *Perfect Puppy v. City of E. Providence*, 98 F. Supp. 3d 408, 415–18 (D.R.I. 2015). *Contra Six Kingdoms Enters. v. City of El Paso*, No. EP-10-CV-485-KC, 2011 WL 65864, at \*8 (W.D. Tex. Jan. 10, 2011) (“By limiting the price of puppies to an amount that sellers of puppies from distant states cannot meet, the ordinance plainly has a discriminatory impact upon out-of-state interests.”).

<sup>27</sup> *N.Y. State Trawlers Ass’n v. Jorling*, 16 F.3d 1303, 1308 (2d Cir. 1994) (citing *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 471–72 (1981)); see also *Automated Salvage Transp. v. Wheelabrator Env’tl. Sys.*, 155 F.3d 59, 75 (2d Cir. 1998) (“Where a regulation does not have this disparate impact on interstate commerce, then ‘we must conclude that . . . [it] has not imposed any “incidental burdens” on interstate commerce that “are clearly excessive in relation to the putative local benefits.”’ Thus, the minimum showing required to succeed in a Commerce Clause challenge to a state regulation is that it have a disparate impact on interstate commerce. The fact that it may otherwise affect commerce is not sufficient.”); *Pac. Nw. Venison Producers v. Smitch*, 20 F.3d 1008, 1015 (9th Cir. 1994) (explaining that “incidental burdens” on interstate commerce include disruption of interstate travel and shipping due to lack of uniformity in state laws, impacts on commerce beyond the borders of the state, or burdens that fall more heavily on out-of-state interests).

<sup>28</sup> *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 127 (1978) (“[T]he Commerce Clause [does not] protect[] the particular structure or methods of operation in a retail market.”).

intrastate commerce”<sup>29</sup> such as to make the statute “unreasonable or irrational.”<sup>30</sup> If no such unequal burden is shown, a reviewing court need not proceed further.<sup>31</sup> Unless a plaintiff demonstrates that the statute imposes some burden on interstate commerce that is different from the burden imposed on intrastate commerce, courts should refrain entirely from weighing a statute’s costs and benefits.<sup>32</sup>

The competency or propriety of courts undertaking these inquiries has been much maligned. The Fourth Circuit has criticized the *Pike* balancing test as “often too soggy to properly cabin the judicial inquiry or effectively prevent the district court from assuming a super-legislative role;”<sup>33</sup> while on the Tenth Circuit, then-Judge Gorsuch called *Pike* “a pretty grand, even ‘ineffable,’ all-things-considered sort of test, one requiring judges (to attempt) to compare wholly incommensurable goods for wholly

<sup>29</sup> National Elec. Mfrs. Ass’n v. Sorrell, 272 F.3d 104, 109 (2d Cir. 2001); see also *Park Pet Shop*, 872 F.3d at 502 (“*Pike* balancing is triggered *only* when the challenged law *discriminates* against interstate commerce in practical application.”) (emphasis in original).

<sup>30</sup> Alaska Airlines v. City of Long Beach, 951 F.2d 977, 983 (9th Cir. 1991). A statute is “unreasonable or irrational . . . where the asserted benefits of the statute are in fact illusory or relate to goals that evidence an impermissible favoritism of in-state industry over out-of-state industry.” *Id.* See also Hunt v. Wash. State Apple Advert. Comm’n, 432 U.S. 333, 353 (1977); Wash. State Apple Advert. Comm’n v. Holshouser, 408 F. Supp. 857, 861 (E.D.N.C. 1976).

<sup>31</sup> *Sorrell*, 272 F.3d at 109. “*Pike* balancing is triggered *only* when the challenged law *discriminates* against interstate commerce in practical application. *Pike* is not the default standard of review for any state or local law that affects interstate commerce.” *Park Pet Shop*, 872 F.3d at 502. “[U]nless the challenged law discriminates against interstate commerce in practical effect, the dormant Commerce Clause does not come into play and *Pike* balancing does not apply.” *Id.* See also Nat’l Paint & Coatings Ass’n v. City of Chicago, 45 F.3d 1124, 1130 (7th Cir. 1995) (rejecting a default application of *Pike* and holding “the dormant [C]ommerce [C]lause does not replace the rational-basis inquiry with a ‘broader, all-weather, be-reasonable vision of the Constitution”).

<sup>32</sup> See Dep’t of Revenue of Ky. v. Davis, 553 U.S. 328, 360 (2008) (Scalia, J., concurring) (“I would abandon the *Pike*-balancing enterprise altogether and leave these quintessentially legislative judgments with the branch to which the Constitution assigns them.”); see also United Haulers Ass’n v. Oneida-Herkimer Solid Waste Mgmt. Auth., 550 U.S. 330, 346 (2007) (noting that the *Pike* balancing test was “reserved” for laws that have incidental effects on interstate commerce, but finding “it unnecessary to decide whether the ordinances impose any incidental burden on interstate commerce because any arguable burden does not exceed the public benefits of the ordinances”); *Exxon Corp.*, 437 U.S. at 125–26 (“Plainly, the Maryland statute [prohibiting producer or refiner of petroleum products from operating retail service station within the State] does not discriminate against interstate goods, nor does it favor local producers and refiners. Since Maryland’s entire gasoline supply flows in interstate commerce and since there are no local producers or refiners, such claims of disparate treatment between interstate and local commerce would be meritless. . . . The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce.”); Brown & Williamson Tobacco Corp. v. Pataki, 320 F.3d 200, 209 (2d Cir. 2003) (“This balancing test, however, does not invite courts to second-guess legislatures by estimating the probable costs and benefits of the statute, nor is it within the competency of courts to do so.”); *Nat’l Paint*, 45 F.3d at 1130 (finding that the dormant Commerce Clause does not “authorize a [court to undertake] a comprehensive review of the law’s benefits, free of any obligation to accept the legislature’s judgment”).

<sup>33</sup> Colon Health Ctrs. of Am. v. Hazel, 733 F.3d 535, 546 (4th Cir. 2013).



different populations (measuring the burdens on out-of-staters against the benefits to in-staters).”<sup>34</sup> Justice Scalia explained this dilemma at greater length in *Davis*:

The burdens and the benefits are always incommensurate, and cannot be placed on the opposite balances of a scale without assigning a policy-based weight to each of them. It is a matter not of weighing apples against apples, but of deciding whether three apples are better than six tangerines. . . . [Y]ou cannot decide which interest “outweighs” the other without deciding which interest is more important to you.<sup>35</sup>

There is “no clear line between these two strands of analysis” and several cases, including *Pike* itself, that have purported to apply the undue burden test “turned in whole or in part on the discriminatory character of the challenged state regulations.”<sup>36</sup> This has led some courts to “wonder just what work *Pike* does”<sup>37</sup> and several scholars suggest that the Supreme Court has “*sub silentio*” repudiated the balancing test by failing to invalidate any laws under it since 1982<sup>38</sup> and “burden review has decayed into minimal rational basis review at best.”<sup>39</sup>

When a state “project[s] its legislation into” other jurisdictions<sup>40</sup> and “directly controls” conduct wholly beyond its borders, whether to punish, reward or otherwise influence, and irrespective of whether it is discriminatory or its extraterritorial reach was intended, the statute is *per se* invalid.<sup>41</sup> Despite the doctrine often being premised on the possibility of inconsistent regulatory regimes if more than one state were to regulate in this space, the actual existence of a conflict

<sup>34</sup> *Energy & Env’t Legal Inst. v. Epel*, 793 F.3d 1169, 1171 (10th Cir. 2015).

<sup>35</sup> *Davis*, 553 U.S. at 360 (Scalia, J., concurring). Scalia, never at a loss for quips, has also compared this inquiry to “judging whether a particular line is longer than a particular rock is heavy.” *Bendix Autolite Corp. v. Midwesco Enters.* 486 U.S. 888, 897 (1988) (Scalia, J., concurring).

<sup>36</sup> *General Motors Corp. v. Tracy*, 519 U.S. 278, 298 n.12 (1997).

<sup>37</sup> *Cavel Int’l v. Madigan*, 500 F.3d 551, 556 (7th Cir. 2007). Some courts, citing a footnote in *Tracy*, 519 U.S. at 298 n.12, have suggested that *Pike* is only violated when a “genuinely nondiscriminatory” state law “undermine[s] a compelling need for national uniformity in regulation.” See *LSP Transmission Holdings v. Lange*, No. CV 17-4490 (DWF/HB), 2018 WL 3075976, at \*9 (D. Minn. June 21, 2018) (finding “[t]he Supreme Court [in this footnote] also noted the narrow application of the *Pike* test”); *Owner-Operator Indep. Drivers Ass’n v. Urbach*, 718 N.Y.S.2d 282, 285 (App. Div. 2000) (“[I]t is incumbent upon plaintiffs to identify some prohibited interference with interstate commerce under the *Pike* undue burden test to obviate the need to establish that their commercial interests have received disparate treatment from those of similarly situated intrastate operators.”). *But see* *Yamaha Motor Corp., U.S.A. v. Jim’s Motorcycle*, 401 F.3d 560, 572 (4th Cir. 2005).

<sup>38</sup> Brannon P. Denning, *Reconstructing the Dormant Commerce Clause Doctrine*, 50 WM. & MARY L. REV. 417, 493 (2008).

<sup>39</sup> Francis, *supra* note 14, at 277.

<sup>40</sup> *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 583 (1986) (quoting *Baldwin v. G.A.F. Seeling*, 294 U.S. 511, 521 (1935)).

<sup>41</sup> *Healy v. Beer Inst.*, 491 U.S. 324, 336–37 (1994).

is not a prerequisite for its application.<sup>42</sup> However, as changes to the global economy blur the line between intrastate and interstate transactions, the doctrine has atrophied.

Extraterritoriality's demise is in part attributable to its birth during an earlier phase of dormant Commerce Clause jurisprudence where the Court found a regulation of interstate commerce permissible based on whether it was a "direct" or "indirect" regulation;<sup>43</sup> the Court's furnishing of alternative grounds for its holding in *MITE* and *Healy* are a recognition of such by its members.<sup>44</sup> As the Court's conception of states' territories have grown more fluid in other areas of law, such as personal jurisdiction<sup>45</sup> and choice-of-law,<sup>46</sup> to reflect the increasingly interconnected world, some have called for it to do so here. Justice Gorsuch's 2015 decision, while still a judge of the Tenth Circuit, in *Energy and Environment Legal Institute v. Epel*,<sup>47</sup> labeled the extraterritoriality doctrine "the most dormant doctrine in dormant [C]ommerce [C]ause jurisprudence"<sup>48</sup> and no longer binding.<sup>49</sup> He suggested that rather than constituting "a distinct line" of dormant Commerce Clause jurisprudence, *Baldwin* and its progeny were examples of the anti-discrimination rule that was yet to solidify.<sup>50</sup> Similarly, Judge Sutton of the Sixth Circuit has

<sup>42</sup> Barbara O. Bruckmann, *The Case for a Commerce Clause Challenge to State Antitrust Laws Banning Minimum Resale Price Maintenance*, 39 HASTINGS CONST. L.Q. 391, 415 (2012) ("[D]irect regulatory conflict appears a sufficient, but not necessary, condition for demonstrating extraterritorial regulation.").

<sup>43</sup> Brannon P. Denning, *Extraterritoriality and the Dormant Commerce Clause: A Doctrinal Post-Mortem*, 73 LA. L. REV. 979, 996 (2013).

<sup>44</sup> *Healy*, 491 U.S. at 340 (striking down a statute because it "discriminate[d] against brewers . . . [who] engaged in interstate commerce"). In his *Healy* concurrence, Justice Scalia labeled the extraterritoriality doctrine "both dubious and unnecessary to decide the present cases." *Id.* at 345 (Scalia, J., concurring). *Edgar v. MITE Corp.*, 457 U.S. 624, 642 (1982) (finding the statute was "a direct restraint on interstate commerce" that would have thoroughly stifled the ability of out-of-state corporations to make tender offers).

<sup>45</sup> *See Int'l Shoe Co. v. Washington*, 326 U.S. 310, 320 (1945) (finding that personal jurisdiction can be established with a nexus-oriented approach).

<sup>46</sup> *See* Jeffrey M. Schmitt, *Making Sense of Extraterritoriality: Why California's Progressive Global Warming and Animal Welfare Legislation Does Not Violate the Dormant Commerce Clause*, 39 HARV. ENVTL. L. REV. 423, 454–55 (2015).

<sup>47</sup> *Energy & Env't Legal Inst. v. Epel*, 793 F.3d 1169 (10th Cir. 2015).

<sup>48</sup> *Id.* at 1170. *See IMS Health Inc. v. Mills*, 616 F.3d 7, 29 n.27 (1st Cir. 2010) ("Extraterritoriality has been the dormant branch of the dormant Commerce Clause."). This outlook is also shared by scholars. *See, e.g.,* Denning, *supra* note 43, at 1006 ("[E]xtraterritoriality is, for all intents and purposes, dead.").

<sup>49</sup> *See Epel*, 793 F.3d at 1173–75. In *Epel*, the court stated:

[S]tate laws setting non-price standards for products sold in-state (standards concerning, for example, quality, labeling, health, or safety) may be amenable to scrutiny under the generally applicable *Pike* balancing test, or scrutinized for traces of discrimination under *Philadelphia*, but the Court has never suggested they trigger near-automatic condemnation under *Baldwin*.

*Id.* at 1173.

<sup>50</sup> *Id.* at 1173.

suggested that “[t]he extraterritoriality doctrine . . . is a relic of the old world with no useful role to play in the new,”<sup>51</sup> whose elimination as a freestanding prohibition would not alter case outcomes.<sup>52</sup> There presently exists a debate amongst the circuits regarding whether *Pharmaceutical Research & Manufacturers of America v. Walsh*,<sup>53</sup> where the Court referred to the doctrine not as “extraterritoriality” but rather “[t]he rule that was applied in *Baldwin* and *Healy*,”<sup>54</sup> limited its principle to price affirmation statutes.<sup>55</sup> Others have suggested that “the extraterritoriality doctrine should apply only when the state directly regulates out-of-state conduct or the state regulates in-state conduct in such a way that it has the inescapable practical effect of regulating out-of-state conduct in which the state has no corresponding interest.”<sup>56</sup>

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<sup>51</sup> *Am. Beverage Ass’n v. Snyder*, 735 F.3d 362, 378 (6th Cir. 2013) (Sutton, J., concurring).

<sup>52</sup> *Id.* at 380–81 (arguing that extraterritoriality was not essential to the holdings in *Healey*, *Brown-Forman*, *Edgar*, or *Baldwin*).

<sup>53</sup> *Pharm. Research & Mfr. of Am. v. Walsh*, 538 U.S. 644, 669 (2003).

<sup>54</sup> *Id.*

<sup>55</sup> *See Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, 729 F.3d 937, 951 (9th Cir. 2013) (“*Healy* and *Baldwin* are not applicable to a statute that does not dictate the price of a product and does not ‘t[ie] the price of its in-state products to out-of-state prices.’”) (internal citation omitted); *Chinatown Neighborhood Ass’n v. Harris*, 794 F.3d 1136, 1145–46 (9th Cir. 2015) (finding “even when state law has significant extraterritorial effects, it passes Commerce Clause muster when, as here, those effects result from the regulation of in-state conduct” and distinguishing *Sam Francis Found. v. Christies, Inc.*, 784 F.3d 1320 (9th Cir. 2015), as “invalidating a . . . statute that ‘facially regulates . . . wholly outside the State’s borders’”) (internal citation omitted); *IMS Health Inc. v. Mills*, 616 F.3d 7, 30 (1st Cir. 2010) (recognizing that the Supreme Court “has only struck down two related types of statutes on extraterritoriality grounds” which include “price affirmation statutes” and “statutes that ‘force an out-of-state merchant to seek regulatory approval in one State before undertaking a transaction in another’”) (internal citation omitted). *But see Ass’n for Accessible Meds. v. Frosh*, 887 F.3d 664, 670 (4th Cir. 2018) (“The Supreme Court’s statement does not suggest that ‘[t]he rule that was applied in *Baldwin* and *Healy*’ applies *exclusively* to ‘price control or price affirmation statutes.’ Instead, the Court’s statement emphasizes that the extraterritoriality principle is violated if the state law at issue ‘regulate[s] the price of any out-of-state transaction, either by its express terms or by its inevitable effect.’”) (internal citation omitted); *North Dakota v. Heydinger*, 825 F.3d 912, 920 (8th Cir. 2016) (finding “[t]he district court correctly noted the Supreme Court has never so limited the [extraterritoriality] doctrine [to price control], and indeed has applied it more broadly,” but declining to address claims that extraterritorial legislation should be analyzed under the *Pike* balancing test or deemed “per se invalid”). This debate predates *Walsh*. *See, e.g., Nat’l Solid Wastes Mgmt. Ass’n v. Meyer*, 63 F.3d 652, 659 (7th Cir. 1995) (“Although cases like *Healy* and *Brown-Forman Distillers Corp.* involved price affirmation statutes, the principles set forth in these decisions are not limited to that context.”).

<sup>56</sup> Schmitt, *supra* note 46, at 449; *see also N.Y. Pet Welfare Ass’n v. City of New York*, 850 F.3d 79, 91–92 (2d Cir. 2017) (“The Commerce Clause, however, does not void every law that causes behavior to change in other states. Rather, the measure of extraterritoriality is whether the Sourcing Law ‘inescapably require[s]’ breeders to operate on the City’s terms even when doing business elsewhere.” (internal citations omitted)); *Nat’l Elec. Mfrs. Ass’n v. Sorrell*, 272 F.3d 104, 111 (2d Cir. 2001) (“[A] decision to abandon the state’s market rests entirely with individual manufacturers based on the opportunity cost of capital, their individual production costs, and what the demand in the

## II. NO COMMERCE IN ANIMAL CRUELTY

Litigation concerning foie gras bans in Chicago and California is illustrative of how the courts have addressed dormant Commerce Clause challenges to statutes governing the sale of food produced through animal cruelty.<sup>57</sup> On April 26, 2006, as part of the omnibus budget bill, the Chicago City Council enacted legislation prohibiting the sale of foie gras in “[a]ll food dispensing establishments.”<sup>58</sup> The preamble to the statute reiterated that under the Illinois constitution, the City “may exercise any power and perform any function relating to its government and affairs including protecting the health, safety and welfare of its citizens” and by “ensuring the ethical treatment of animals, who are the source of the food offered in our restaurants, the City of Chicago is able to continue to offer the best in dining experiences.”<sup>59</sup> Immediately after adoption, the Illinois Restaurant Association and Allen’s New American Cafe sued in state court.<sup>60</sup> They contended that:

[T]he Ordinance has nothing to do with health, safety, environmental issues or governmental revenue generation. Nor does it fit into traditional areas of state governmental interest in food regulation since there is no tradition in Illinois of banning, on morality and reputational grounds, food that has already been found safe on the federal level for human consumption.<sup>61</sup>

The district court found for Chicago and held that the law did not discriminate against interstate commerce in purpose or effect since it did “not force out-of-state foie gras producers or distributors to do anything.”<sup>62</sup> The court found that “the dormant Commerce Clause

state will bear. Because none of these variables is controlled by the state in this case, we cannot say that the choice to stay or leave has been made for manufacturers by the state legislature, as the Commerce Clause would prohibit.”; *cf. Walsh*, 538 U.S. at 669 (limiting extraterritoriality doctrine to instances where a statute “by its express terms or inevitable effect” regulates extraterritorially).

<sup>57</sup> See generally Kristin Cook, *The Inhumanity of Foie Gras Production—Perhaps California and Chicago Have the Right Idea*, 2 J. ANIMAL L. & ETHICS 263, 263, 269–72 (2007); Rafi Youatt, *Power, Pain, and the Interspecies Politics of Foie Gras*, 65 POL. RES. Q. 346, 346 (2011).

<sup>58</sup> CHICAGO, ILL., MUN. CODE §§ 7-39-001–005 (2006), *Amendment of Title 7, Chapter 39 of Muni. Code of Chicago by Addition of New Sections 001 and 005 Prohibiting Sale of Foie Gras by Food Establishments Before the Comm. on Health*, (Apr. 26, 2006) (repealed May 14, 2008).

<sup>59</sup> MARK CARP, *THE FOIE GRAS WARS: HOW A 5,000-YEAR-OLD DELICACY INSPIRED THE WORLD’S FIERCEST FOOD FIGHT* 127 (2009).

<sup>60</sup> After the plaintiffs amended their complaint to include a dormant Commerce Clause challenge, the city removed the case to federal court. See *Ill. Rest. Ass’n v. City of Chicago*, No. 06 C 7014, 2007 WL 541926, at \*1 (N.D. Ill. Feb. 12, 2007).

<sup>61</sup> Plaintiffs’ Surreply Addressing New United States Supreme Court Decision, at 3, *Ill. Rest. Ass’n v. City of Chicago*, 492 F. Supp. 2d 891 (N.D. Ill. 2007) (No. 06 C 7014), 2007 WL 1973283, at \*3.

<sup>62</sup> *Ill. Rest. Ass’n v. City of Chicago*, 492 F. Supp. 2d 891, 899 (N.D. Ill. 2007).

applies to [facially] nondiscriminatory laws only where the law has some sort of discriminatory effect or when judicial intervention is necessary to promote national uniformity and thereby prevent discrimination,”<sup>63</sup> or citing the words of the Seventh Circuit in *National Paint*,<sup>64</sup> “[n]o disparate treatment, no disparate impact, no problem under the dormant [C]ommerce [C]ause,”<sup>65</sup> and therefore the court was not required to apply *Pike*.<sup>66</sup> The existence of the *Pike* balancing test was not an excuse for the court to engage in “general-purpose balancing” and the court must look for “discrimination rather than for baleful effects.”<sup>67</sup> The court did acknowledge however that its decision was “in tension with other Supreme Court and Seventh Circuit cases which do not delve into the details of the dormant Commerce Clause.”<sup>68</sup> Feeling that the ordinance infringed on freedom of choice and made a national embarrassment of Chicago,<sup>69</sup> the Council repealed the law just over two years later on May 14, 2008,<sup>70</sup> while an appeal was pending before the Seventh Circuit.<sup>71</sup> *Illinois Restaurant Association* found that the regulation of foie gras was not a subject requiring national uniformity and by treating in-state and interstate interests the same, the dormant Commerce Clause was not implicated and balancing was not warranted.<sup>72</sup>

The California statute, while older in origin, remains the subject of litigation. In 2004, California adopted new provisions

<sup>63</sup> *Id.* at 905. The Court also noted that “*United Haulers . . .* is yet another case that recites the *Pike* standard in connection with a facially nondiscriminatory law but, in the same breath, looks to whether the law has any discriminatory effects.” *Id.* See also Francis, *supra* note 14, at 298 (“Analysis of whether a subject ‘requires’ a uniform national standard . . . often seems to be a euphemism for burden review, rooted in a practical economic assessment of the consequences of unilateral state regulation.”); Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris, 729 F.3d 937, 952 (9th Cir. 2013) (“[E]xamples of ‘courts finding uniformity necessary’ fall into the categories of ‘transportation’ or ‘professional sports league[s].’” (internal citation omitted)).

<sup>64</sup> *Nat’l Paint & Coatings Ass’n v. City of Chicago*, 45 F.3d 1124, 1132 (7th Cir. 1995).

<sup>65</sup> *Id.*

<sup>66</sup> See *id.*

<sup>67</sup> *Ill. Rest. Ass’n*, 492 F. Supp. 2d at 904 (quoting *Nat’l Paint*, 45 F.3d at 1131).

<sup>68</sup> *Id.* at 903–04 (referencing *Alliant Energy Corp., Or. Waste Sys., and Clover Leaf*).

<sup>69</sup> See Nick Fox, *Chicago Overturns Foie Gras Ban*, N.Y. TIMES: DINER’S J. (May 14, 2008), <http://dinersjournal.blogs.nytimes.com/2008/05/14/chicago-overturns-foie-gras-ban/> [<http://perma.cc/949N-TE7A>] (“[T]he ban has been a source of embarrassment for the city and the repeal comes as residents have accused officials of trying to micromanage people’s lives . . .”); see also Phil Vettel, *Hold the Jokes the Rest of Yours: Foie Gras Back on Menus*, CHI. TRIB. (May 18, 2008), [http://articles.chicagotribune.com/2008-05-18/news/0805170435\\_1\\_foie-gras-terrine-chicagoans](http://articles.chicagotribune.com/2008-05-18/news/0805170435_1_foie-gras-terrine-chicagoans) [<http://perma.cc/C6E9-JKBG>] (“Ald. Bernard Stone (50th) quickly recanted his support of the ban, saying, ‘Anybody who has traveled anywhere in this country knows that people are just laughing their heads off at us.’”).

<sup>70</sup> See CHICAGO, ILL., MUN. CODE §§ 7-39-001–005 (2006) (adopted Apr. 26, 2006), repealed by Chicago, Ill., Ordinance 2008-2041 (May 14, 2008).

<sup>71</sup> See *Ill. Rest. Ass’n v. City of Chicago*, No. 06 C 7014, 2008 WL 8915042, at \*1, (N.D. Ill. Aug. 7, 2008).

<sup>72</sup> See *Ill. Rest. Ass’n v. City of Chicago*, 492 F. Supp. 2d 891, 905–06 (N.D. Ill. 2007).



of the California Health & Safety Code (sections 25981 and 25982) which prohibited the practice of force-feeding ducks or geese to produce foie gras, as well as the in-state sale of products made elsewhere from force-fed fowl.<sup>73</sup> On July 2, 2012, the day after the state law took effect, Association des Éleveurs de Canards et d'Oies du Québec (hereafter “Canadian Farmers”), a Canadian nonprofit which raises birds for foie gras, sued the state of California (*Association des Éleveurs I*). The Canadian Farmers argued that California’s ban on the sale of foie gras violated the extraterritoriality doctrine because “the practical effect—and perhaps the very purpose—of section 25982 is to project California’s preferred agricultural practices on farmers outside the state.”<sup>74</sup> They contended that the law imposed a burden on the poultry market without any corresponding local benefit because “not a single duck or goose in California is protected by applying section 25982 to . . . ducks and geese born, raised, and slaughtered entirely outside the state.”<sup>75</sup> These claims were rejected as meritless by both the district court<sup>76</sup> and Ninth Circuit,<sup>77</sup> with the latter observing that “[p]laintiffs give us no reason to doubt that the State believed that the sales ban . . . may discourage the consumption of products produced by force feeding birds and prevent complicity in a practice that is deemed cruel to animals.”<sup>78</sup> The appellate court declined to conduct an analysis under *Pike* of whether the statute’s benefits were illusory because the plaintiffs had failed to demonstrate a significant burden on interstate commerce.<sup>79</sup> The law did not prohibit the sale of foie gras, merely the most profitable method of production and “the dormant Commerce Clause does not . . . guarantee [p]laintiffs their preferred method of operation.”<sup>80</sup> Plaintiffs also “failed to show that the foie

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<sup>73</sup> See CAL. HEALTH & SAFETY CODE §§ 25981–25982 (West 2018).

<sup>74</sup> Appellants’ Opening Brief at 20, *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, No. 12-56822, 2012 WL 5915406, at \*20 (9th Cir. Nov. 16, 2012).

<sup>75</sup> *Id.* at \*22.

<sup>76</sup> *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, No. 2:12-CV-05735-SVW-RZ, 2012 WL 12842942, at \*10 (C.D. Cal. Sept. 28, 2012) (“Preventing animal cruelty in California is clearly a legitimate state interest . . . and Plaintiffs have presented no evidence that Section 25982 is an ineffective means of advancing that goal. Plaintiffs have thus failed to raise a serious question that Section 25982’s burden on interstate commerce ‘clearly exceeds’ its local benefits.”).

<sup>77</sup> *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, 729 F.3d 937, 948–52 (9th Cir. 2013) (observing section 25982 is not discriminatory and does not directly regulate or substantially burden interstate commerce).

<sup>78</sup> *Id.* at 952 (citing *Empacadora de Carnes de Fresnillo, S.A. de C.V. v. Curry*, 476 F.3d 326, 336 (5th Cir. 2007) (concluding that ban on slaughter and sale of horsemeat for human consumption may “increase the preservation of horses” by “removing the significant monetary incentives”)).

<sup>79</sup> See *id.* at 951–52 (citing *Nat’l Ass’n of Optometrists & Opticians v. Harris*, 682 F.3d 1144, 1155 (9th Cir. 2012)).

<sup>80</sup> *Id.* at 949 (citing *Nat’l Ass’n of Optometrists*, 682 F.3d at 1151).



gras market is inherently national or that it requires a uniform system of regulation”<sup>81</sup> or any existing competing legislation indicating balkanization. The Supreme Court “has never invalidated a state or local law under the dormant Commerce Clause based upon mere speculation about the possibility of conflicting legislation.”<sup>82</sup> The Supreme Court denied the foie gras companies’ petition for certiorari on October 14, 2014.<sup>83</sup> *Association des Éleveurs I* found the statute barred how, but not where, an item is produced, and therefore *Pike* balancing was unnecessary.

Indeed, not a single animal cruelty statute challenged on Commerce Clause grounds has been struck down on that basis. This includes bans on horsemeat for human consumption upheld by the Fifth and Seventh Circuits,<sup>84</sup> and the Ninth Circuit decision upholding California’s ban on the sale or distribution of shark fins.<sup>85</sup> This also includes two statutes arguably regulating production methods: A California ban on the slaughter of non-ambulatory animals challenged on dormant Commerce Clause grounds but

<sup>81</sup> *Id.* at 952.

<sup>82</sup> *Id.* at 951 (quoting *S.D. Myers, Inc. v. City of San Francisco*, 253 F.3d 461 (9th Cir. 2001)).

<sup>83</sup> See *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, 135 S. Ct. 398 (2014) *cert. denied*. Subsequently, the plaintiffs amended their complaint in the district court seeking declaratory relief asserting that section 25982 was preempted by the Poultry Products Inspection Act (PPIA). *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Harris*, 79 F. Supp. 3d 1136, 1139 (C.D. Cal. 2015). The district court found that the PPIA expressly preempted section 25982 and granted the motion for partial summary judgment while declining to reach any of the other arguments. See *id.* at 1147–48. The Ninth Circuit reversed and vacated in part, finding that the foie gras statute was not preempted by the PPIA expressly or under the doctrines of field or obstacle preemption, and remanded the proceedings. See *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Becerra*, 870 F.3d 1140, 1146, 1153 (9th Cir. 2017). On March 9, 2018, a petition for certiorari was docketed by the plaintiffs and a Call for the Views of the Solicitor General by the Court was issued on June 18, 2018 to which he responded on December 5, 2018 recommending denial. See *Petition for Writ of Certiorari, Ass’n des Éleveurs de Canards et d’Oies du Québec v. Becerra*, No. 17A793 (U.S. Mar. 9, 2018); see also *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Becerra*, 138 S. Ct. 2668 (2018) (mem.), Brief for United States as Amicus Curiae, *Ass’n des Éleveurs de Canards et d’Oies du Québec v. Becerra*, No. 17A793.

<sup>84</sup> See *Empacadora de Carnes de Fresnillo, S.A. de C.V., v. Curry*, 476 F.3d 326, 335 (5th Cir. 2007); *Cavel Int’l v. Madigan*, 500 F.3d 551, 544–55 (7th Cir. 2007).

<sup>85</sup> See *Chinatown Neighborhood Ass’n v. Harris*, 794 F.3d 1136, 1147 (9th Cir. 2015). The court upheld a finding by the district court that “given that the Shark Fin Law is facially neutral, and treats all shark fins the same, regardless of their origin, plaintiffs have not shown (and cannot show) that the Shark Fin Law either regulates extraterritorially, or discriminates in favor of in-state interests.” *Chinatown Neighborhood Ass’n v. Brown*, No. C 12-3759 PJH, 2013 WL 60919, at \*8 (N.D. Cal. Jan. 2, 2013). Finding that the animal cruelty and the health and conservation benefits of the law outweighed the insignificant commercial burden on interstate commerce, the court held in the absence of a significant burden, it would be inappropriate for them “to determine [its] constitutionality . . . based on our assessment of the benefits of th[e] law [ ] and the State’s wisdom in adopting [it],” or the availability of less-burdensome alternatives. *Chinatown Neighborhood Ass’n*, 794 F.3d at 1147 (citing *Nat’l Ass’n of Optometrists & Opticians v. Harris*, 682 F.3d 1144, 1156–57 (9th Cir. 2012)). The Ninth Circuit further discounted the extraterritorial claims saying such effects only are violative when states attempt to fix prices beyond their borders. *Id.* at 1146.

ultimately struck down by the Court for Federal Meat Inspection Act (FMIA) preemption,<sup>86</sup> and a New York statute prohibiting the sale of wild birds not raised in captivity upheld by the Second Circuit.<sup>87</sup>

### III. PROPOSITION 2 AND AB 1437: CALIFORNIA EGGS ON THE STATES

After a voter-initiated initiative campaign, on November 4, 2008, California, by a margin of 63.5% to 36.5%,<sup>88</sup> passed Proposition 2 which required “calves raised for veal, egg-laying hens and pregnant pigs be confined only in ways that allow these animals to lie down, stand up, fully extend their limbs and turn around freely” by 2015.<sup>89</sup> In 2010, the California legislature enacted AB 1437 which banned the sale within the state of eggs from out-of-state farms unless those farmers subjected themselves to the same confinement standards.<sup>90</sup> In adopting the latter, the legislature, in their stated purpose, sought to “protect California consumers from the deleterious, health, safety, and welfare effects of the sale and consumption of eggs derived from egg-laying hens that are exposed to significant stress and many result in increased exposure to disease pathogens including salmonella.”<sup>91</sup>

Even before taking effect, Proposition 2 and AB 1437 spawned numerous lawsuits challenging the ordinances.<sup>92</sup> In 2012, the first

<sup>86</sup> See *Nat'l Meat Ass'n v. Harris*, 565 U.S. 452, 468 (2012).

<sup>87</sup> See *Cresenzi Bird Imps. v. New York*, 831 F.2d 410 (2d Cir. 1987) (affirming the opinion below). “New York has a legitimate interest in regulating its local market conditions which lead, in a short causal chain, to the unjustifiable and senseless suffering and death of thousands of captured wild birds.” *Cresenzi Bird Imps. v. New York*, 658 F. Supp. 1441, 1447 (S.D.N.Y. 1987) (internal citation omitted).

<sup>88</sup> *Votes For And Against November 4, 2008, State Ballot Measures*, CAL. BOARD OF ELECTIONS, [http://elections.cdn.sos.ca.gov/sov/2008-general/7\\_votes\\_for\\_against.pdf](http://elections.cdn.sos.ca.gov/sov/2008-general/7_votes_for_against.pdf) [<http://perma.cc/MTD7-Z4Y3>]; see also Cal. Sec'y of State, *Prevention of Farm Animal Cruelty Act*, in CALIFORNIA GENERAL ELECTION: OFFICIAL VOTER INFORMATION GUIDE 16 (2008), <http://vig.cdn.sos.ca.gov/2008/general/pdf-guide/vig-nov-2008-principal.pdf> [<http://perma.cc/ED6V-EKNK>].

<sup>89</sup> Attorney General, *Prop 2 Standards For Confining Farm Animals. Initiative Statute*, CAL. GENERAL ELECTION (Nov. 4, 2008), <http://vigarchive.sos.ca.gov/2008/general/title-sum/prop2-title-sum.htm> [<http://perma.cc/FZJ8-BA5W>]; see also Letter from Joe Ramsey to Toni Melton, Initiative Coordinator, Office of the Attorney Gen., Request for Title and Summary for Proposed Initiative (Aug. 9, 2007), [http://ag.ca.gov/cms\\_pdfs/initiatives/2007-08-09\\_07-0041\\_Initiative.pdf](http://ag.ca.gov/cms_pdfs/initiatives/2007-08-09_07-0041_Initiative.pdf) [<http://perma.cc/DCD3-CNS7>].

<sup>90</sup> 2010 Cal. Stat. 51. On November 6, 2018, California voters approved Proposition 12 replacing the Proposition 2 size restrictions based on animal behavior with specific numbers of square feet and ban the sale of non-conforming veal and pork as of 2020. *California Election Results*, NEW YORK TIMES, Nov. 6, 2018, <https://www.nytimes.com/interactive/2018/11/06/us/elections/results-california-elections.html>; Letter from Cheri Shankar, to Ashley Johansson, Initiative Coordinator, Request For Title and Summary of Proposed Initiative (Aug. 29, 2017), [https://www.oag.ca.gov/system/files/initiatives/pdfs/17-0026%20%28Animal%20Cruelty%29\\_0.pdf](https://www.oag.ca.gov/system/files/initiatives/pdfs/17-0026%20%28Animal%20Cruelty%29_0.pdf) [<http://perma.cc/2FC7-2YUP>].

<sup>91</sup> CAL. HEALTH & SAFETY CODE § 25995(e) (West 2018).

<sup>92</sup> See, e.g., *JS West Milling Co. v. State*, No. 10-CECG-04225 (Cal. Super. Ct. Oct. 14, 2011) (dismissing on ripeness grounds the allegations that Proposition 2 was unconstitutionally

federal suit was brought by a California egg farmer, William Cramer, who challenged the Proposition 2 cage size requirement as unconstitutionally vague under the Fourteenth Amendment's Due Process Clause, because it did not identify satisfactory cage specifications,<sup>93</sup> and as violating the Commerce Clause by forcing the closure and relocation of California egg farmers which in turn would lead to increased consumer prices and disruption of the national corn feed market.<sup>94</sup> The district court dismissed the claims, finding that the law was not vague but rather established a clear test that “does not require the law enforcement officer to have the investigative acumen of Columbo”<sup>95</sup> and that Cramer’s “factual allegations are wholly insufficient to raise his [Commerce Clause] claim above the speculative level”<sup>96</sup> since, as the plaintiff acknowledged, “the prevention of animal cruelty is a legitimate state interest.”<sup>97</sup> After Cramer appealed, the Ninth Circuit, without hearing oral arguments, affirmed the motion to dismiss in a brief, unpublished February 2015 opinion which only addressed the void for vagueness claim and made no mention of the Commerce Clause.<sup>98</sup>

In February 2014, Missouri filed suit,<sup>99</sup> alleging AB 1437 violated the Commerce and Supremacy Clauses of the United States Constitution and were further “expressly and implicitly preempted by the federal Egg Products Inspection Act” (EPIA).<sup>100</sup> The district court dismissed the suit for lack of standing in October 2014, finding it “patently clear” the plaintiffs were “bringing this action on behalf of a subset of each state’s egg farmers and their purported right to participate in the laws that govern them, not on behalf of each state’s population generally.”<sup>101</sup> The Ninth Circuit affirmed the dismissal, finding that “[t]he complaint contain[ed] no

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vague because it did not specify compliant cage dimensions); Ass’n of Calif. Egg Farms v. State, No. 12-CECG-03695-DSB, 2013 WL 9668707, at \*4 (Cal. Super. Ct. Aug. 22, 2013) (finding that definition of confinement standards in terms of “animal behaviors rather than in square inches” did not make Proposition 2 facially vague). *See also*, Molly L. Wiltshire, *Of Eggs and Hens: Pro Bono Opportunities in the Area of Animal Law*, SCHIFF HARDIN (Jan. 1, 2017), <https://www.schiffhardin.com/insights/publications/2016/of-eggs-and-hens-pro-bono-opportunities-in-the-area-of-animal-law> [<http://perma.cc/T39C-JQTV>].

<sup>93</sup> Complaint for Declaratory and Injunctive Relief at 5, *Cramer v. Brown*, (No. CV 12 - 03130 JFW (JEMx)), 2012 WL 1230649 (C.D. Cal. Apr. 10, 2012).

<sup>94</sup> *Id.* at 6.

<sup>95</sup> *Cramer v. Brown*, No. CV123130JFWJEMX, 2012 WL 13059699, at \*4 (C.D. Cal. Sept. 12, 2012).

<sup>96</sup> *Id.* at \*5.

<sup>97</sup> *Id.* (“[T]he prohibition of animal cruelty itself has a long history in American law, starting with the early settlement of the Colonies.” (citing *United States v. Stevens*, 559 U.S. 460, 469 (2010))).

<sup>98</sup> *See Cramer v. Harris*, 591 F. App’x 634, 635 (9th Cir. 2015).

<sup>99</sup> *See Missouri v. Harris*, 58 F. Supp. 3d 1059, 1063 (E.D. Cal. 2014) (five other states—Alabama, Kentucky, Iowa, Oklahoma and Nebraska—subsequently joined the suit).

<sup>100</sup> *Id.* at 1065; 21 U.S.C. § 1031 (2018).

<sup>101</sup> *Harris*, 58 F. Supp. 3d at 1078.

specific allegations about the statewide magnitude of [the alleged difficult choices engendered by the law] or the extent to which they affect[ed] more than just an ‘identifiable group of individual’ egg farmers”<sup>102</sup> and “the unavoidable uncertainty of the alleged future changes in price ma[de] the alleged injury insufficient for Article III standing.”<sup>103</sup> A petition for certiorari was denied by the Supreme Court in May 2017.<sup>104</sup>

In December 2017, the plaintiff States, with the exception of Kentucky, and joined by Arkansas, Indiana, Louisiana, Nevada, North Dakota, Oklahoma, Texas, Utah and Wisconsin, filed an original jurisdiction action with the Supreme Court.<sup>105</sup> The motion alleged AB 1437 was motivated by economic protectionism, relying at least in part on Governor Schwarzenegger’s signing statement: “[b]y ensuring that all eggs sold in California meet the requirements of Proposition 2, this bill is good for both California egg producers and animal welfare.”<sup>106</sup> The plaintiff States contend that AB 1437 “has not provided any significant health-and-safety benefits to Californians” or other persons and the “recited purpose was pretextual” with “no convincing scientific evidence” of correlation between salmonella incidence or stress levels and cage size or stocking density.<sup>107</sup> Rather, they asserted the statute “was designed to impose onerous restrictions on out-of-state egg producers to . . . eliminate any competitive disadvantage to California producers arising from California’s stifling regulatory environment.”<sup>108</sup> Under their reading, AB 1437 “did not affect the welfare of any animal in California” nor did it “regulate any activity within California” but rather “applies only to egg production occurring outside California, and its direct impact is exclusively extraterritorial to California.”<sup>109</sup> Relying on the record from the legislative deliberations,<sup>110</sup> the plaintiff States asserted “[t]he sole

<sup>102</sup> *Missouri ex rel. Koster v. Harris*, 847 F.3d 646, 652 (9th Cir. 2017), *cert. denied sub nom. Missouri ex rel. Hawley v. Becerra*, 137 S. Ct. 2188 (2017) (quoting Alfred L. Snapp & Son v. Puerto Rico *ex rel. Barez*, 458 U.S. 592, 607 (1982)).

<sup>103</sup> *Id.* at 653.

<sup>104</sup> *See* Hawley, 137 S. Ct. at 2188.

<sup>105</sup> Motion For Leave To File Bill Of Complaint, *Missouri v. California*, No. 220148 (U.S. Dec. 4, 2017).

<sup>106</sup> LEG. OF CAL., ASSEMB. J., Reg. Sess., vol. 5, at 5961 (2009–2010).

<sup>107</sup> Motion For Leave To File Bill of Complaint, *supra* note 105, at 18.

<sup>108</sup> *Id.* at 19.

<sup>109</sup> *Id.* at 20. *See also* Brief of Ass’n. Des Éleveurs De Canards Et D’oies Du Québec, HVFG L.L.C., and Hot’s Rest. Grp., as *Amici Curiae* in Support of Plaintiffs at 8, *Indiana v. Massachusetts*, No. 220149 (“If any of the farm animals at issue in these cases feel any discomfort, they do so far beyond California’s borders — and thus far beyond the State’s legitimate legislative reach.”).

<sup>110</sup> “The intent of this legislation is to level the playing field so that in-state producers are not disadvantaged.” Kevin De Leon, CAL. ASSEMB. COMM. ON APPROPRIATIONS, BILL ANALYSIS OF AB 1437, at 1 (May 13, 2009), [http://www.leginfo.ca.gov/pub/09-10/bill/asm/ab\\_14011450/ab\\_1437\\_cfa\\_20090512\\_182647\\_asm\\_comm.html](http://www.leginfo.ca.gov/pub/09-10/bill/asm/ab_14011450/ab_1437_cfa_20090512_182647_asm_comm.html) [<http://perma.cc/9UFY-BKB2>].

purpose and effect of AB 1437 was to regulate the conduct of egg producers outside California.”<sup>111</sup> Additionally, they contended “California affronts the sovereignty of Plaintiff States” by dispatching inspectors to farms within their borders.<sup>112</sup>

In its response papers, California noted that “[b]oth Proposition 2 and AB 1437 address activities occurring within California” and “AB 1437 applies uniformly (and only) to in-state sales, wherever the eggs may have been produced.”<sup>113</sup> It distinguished AB 1437 from the price-control laws struck down in *Healey*, *Brown-Forman*, and *Baldwin* as “indifferent to how eggs sold in other States are produced or priced.”<sup>114</sup> In response to the plaintiff States’ allegations about legislative intent to “level the playing field,” California argued that:

[T]he dormant Commerce Clause forbids States from adopting measures that *privilege* in-state companies at the expense of out-of-state ones. The Constitution does not require a State to confer preferential treatment on out-of-state entities that choose to sell their products within that State, or to exempt those entities from the same neutral rules that apply to in-state sellers.<sup>115</sup>

#### IV. THIRTEEN STATES HAVE A COW WHEN MASSACHUSETTS GOVERNS VEAL

On November 8, 2016, Massachusetts, at a public referendum by a margin of 77.7% to 22.3%,<sup>116</sup> adopted “An Act to Prevent Cruelty to Farm Animals” which prohibited the sale in Massachusetts, after January 1, 2022, of certain eggs, veal, and pork based on the conditions in which the animals were confined.<sup>117</sup> The stated primary purpose of the legislation was “to prevent animal cruelty by phasing out extreme methods of farm animal confinement which also threaten the health and safety of Massachusetts consumers, increase the risk of foodborne illness, and have negative fiscal impacts on the Commonwealth of Massachusetts.”<sup>118</sup> In December 2017, Indiana, joined by Alabama, Arkansas, Louisiana, Missouri, Nebraska, North Dakota, Oklahoma, South Carolina, Texas, Utah, West Virginia, and Wisconsin filed

<sup>111</sup> Reply Brief of Plaintiff States at 5–6, *Missouri v. California*, No. 22O148 (U.S. Mar. 20, 2018).

<sup>112</sup> *Id.*

<sup>113</sup> Brief in Opposition at 1, *Missouri v. California*, No. 22O148 (U.S. Mar. 5, 2018).

<sup>114</sup> *Id.* at 23.

<sup>115</sup> *Id.* at 24–25.

<sup>116</sup> See *An Act to Prevent Cruelty to Animals*, VOTE SMART: FACTS MATTER, <https://votesmart.org/elections/ballot-measure/2184/an-act-to-prevent-cruelty-to-farm-animals#W6FtVehKg2w> [http://perma.cc/G883-HRS6].

<sup>117</sup> *An Act to Prevent Cruelty to Farm Animals*, ch. 333 (Mass. 2016), <https://malegislature.gov/Laws/SessionLaws/Acts/2016/Chapter333> [http://perma.cc/8PBF-LZR5].

<sup>118</sup> *Id.*



suit before the Supreme Court.<sup>119</sup> The plaintiff States sought to distinguish the justification of the “Animal Law” by reference to “the conditions of production simpliciter” from previously upheld laws concerning the quality of the products.<sup>120</sup> They contended that, “while *Pike* balancing is appropriate where states regulate interstate commerce as part of a legitimate attempt to protect the health and safety of citizens, it does not apply where a state is simply trying to export its preferred public policy to other states.”<sup>121</sup> They asserted the law “constitutes economic protectionism and extraterritorial regulation” because “farmers in Plaintiff States must now submit to Massachusetts’s laws, as well as those of any state that adopts similar regulations, in order to have access to those states’ markets.”<sup>122</sup> “[W]hile Massachusetts may legitimately protect its consumers from harmful foodstuffs produced elsewhere, it may not leverage access to its markets to regulate every station in the supply chain of agricultural commodities.”<sup>123</sup> The plaintiff states in the Massachusetts litigation argued that the regulations would force out-of-state farming operations to “alter their production methods with respect to commercial activities occurring wholly outside” Massachusetts and were “not directed at the quality of covered products but rather at the means or characteristics of production of such covered products.”<sup>124</sup>

In its papers, Massachusetts countered that the plaintiff States’ dormant Commerce Clause claims were “foreclosed by centuries of precedent”<sup>125</sup> and the State’s legitimate interests in regulating its food supply outweighed any incidental burden on interstate commerce.<sup>126</sup> Attorney General Maura Healey asserted that Massachusetts was “plac[ing] no special ‘burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear”<sup>127</sup> and took particular note that the statute only governs sales where the buyer took physical possession within Massachusetts, allowing noncompliant food products, and animals

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<sup>119</sup> Motion For Leave To File A Bill Of Complaint, *Indiana v. Massachusetts*, No. 22O149 (U.S. Dec. 11, 2017).

<sup>120</sup> Reply in Support of Motion for Leave to File Bill of Complaint at 4–5, *Indiana v. Massachusetts*, No. 22O149 (U.S. Mar. 19, 2018).

<sup>121</sup> *Id.* at 6.

<sup>122</sup> Bill of Complaint at 13, *Indiana v. Massachusetts*, No. 22O149 (U.S. Dec. 11, 2017).

<sup>123</sup> Brief in Support of Motion for Leave to File Bill of Complaint at 6, *Indiana v. Massachusetts*, No. 22O149 (U.S. Dec. 11, 2017).

<sup>124</sup> Bill of Complaint, *supra* note 122, at 13.

<sup>125</sup> Brief in Opposition to Motion for Leave to File Complaint at 2, *Indiana v. Massachusetts*, No. 22O149 (U.S. Mar. 5, 2018).

<sup>126</sup> *Id.* at 27 (citing *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970)).

<sup>127</sup> *Id.* at 28 (citing *Am. Trucking Ass’n v. Mich. Pub. Serv. Comm’n*, 545 U.S. 429, 433 (2005)).



in cages noncompliant with the minimum-size requirements, to travel freely across its borders if bound for another state.<sup>128</sup>

#### V. FEDS: CASES DON'T MEAT STANDARDS FOR GRANT

On April 16, 2018, the Supreme Court issued Calls for the Views of the Solicitor General (CVSGs) in both cases.<sup>129</sup> The Solicitor General responded on November 29th, recommending denial of the motions for leave.<sup>130</sup> While the majority of the filings focused on the inappropriateness of the cases for an exercise of original jurisdiction as no direct economic injury by the defendant states had been shown,<sup>131</sup> the government also argued that the laws were not violative of the Dormant Commerce Clause.<sup>132</sup> The statutes did not discriminate as they treated all products alike without any local preference,<sup>133</sup> and assessing the health and safety rationales under *Pike* or “whether the practical effect of the regulation is to control conduct beyond the boundaries of the state” would require resolution of complex factual issues best undertaken by the district courts.<sup>134</sup> Additionally, the Solicitor General argued that the EPIA did not preempt the California ordinance since the USDA egg-grading standards do not address confinement conditions.<sup>135</sup>

Of note in their papers, the government declined to address the permissible scope of a cruelty rationale, suggested that even in the absence of discrimination a *Pike* analysis is necessary, and, possibility in a nod to Gorsuch,<sup>136</sup> called “extraterritoriality” not that name, but rather, as “*Baldwin* and its progeny,” which it characterized as “forbidding States from attempting to regulate the price of products sold in another State.”<sup>137</sup>

#### VI. HATCHING CONCLUSIONS

The confinement statutes, which apply equally to in-state and out-of-state farmers, implicate neither of the concerns

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<sup>128</sup> *Id.* at 28–29.

<sup>129</sup> *Missouri v. California*, 138 S. Ct. 1585 (2018) (mem.); *Indiana v. Massachusetts*, 138 S. Ct. 1585 (2018) (mem.).

<sup>130</sup> Brief for United States as Amicus Curiae, *Indiana v. Massachusetts*, No. 220149; Brief for United States as Amicus Curiae, *Missouri v. California*, No. 220148.

<sup>131</sup> *See* Brief for United States as Amicus Curiae, *Missouri v. California*, No. 220148, at \*8–18.

<sup>132</sup> *Id.* at \*20–22.

<sup>133</sup> *See id.* at \*21.

<sup>134</sup> *See id.* at \*21–22.

<sup>135</sup> *Id.* at \*7.

<sup>136</sup> *See Energy & Env't Legal Inst. v. Epel*, 793 F.3d 1169 (10th Cir. 2015).

<sup>137</sup> *See supra* note 131, at \*22.

animating modern Supreme Court dormant Commerce Clause jurisprudence: intentional economic protectionism or the imposition of undue burdens.<sup>138</sup> The California and Massachusetts legislatures and electorates respectively have made a policy determination that the animal welfare and related public health rationales for prohibiting the sale of products not satisfying their confinement standards outweigh any economic impacts or interests in those choices. These determinations of the public interest—that so confined animals are not suitable for consumption—have already been made and since neither statute inescapably requires any business to alter their practices and conduct business in other states in conformity with their regulations, or precludes any other state from regulating these products in a different manner, there is no justification nor need for the Court to assert its views over them.

The California and Massachusetts statutes share many attributes and therefore can be considered jointly for the purposes of repudiating the extraterritorial attacks on their validity. However, despite the lack of treatment by the Solicitor General, the unique adoption of AB 1437 sets California apart for the purposes of assessing the presence of discrimination. While AB 1437 does not favor California egg farmers, it does benefit them by placing out-of-state producers on equal footing. Some have asked “whether the dormant Commerce Clause requires discrimination against in-state producers”<sup>139</sup> and the plaintiff States’ argument would fault California for their political process—if they had passed AB 1437 without previously passing Prop. 2 it would not be susceptible to challenge as protectionist. Even though a benefit inures to in-state interests by the similar burdening of interstate commerce with regulations to which the former is already subject, the treatment is not differential and therefore ipso facto not discriminatory. AB 1437 does not refer specifically to out-of-state farms and so is a non-discriminatory statute, notwithstanding the pre- and ongoing existence of Prop. 2, which the legislature is unable to formally reconcile because of constitutional prohibitions.<sup>140</sup>

Protectionist bans, even if partial, are “local measures for control and suppression of the problem [that] are in force [and] are

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<sup>138</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2091 (2018).

<sup>139</sup> David M. Driesen, *Must the States Discriminate Against Their Own Producers Under the Dormant Commerce Clause?*, 54 HOUS. L. REV. 1, 6 (2016). See also *Nat'l Audubon Soc'y v. Davis*, 307 F.3d 835, 857 (9th Cir. 2002) (“To the extent that Proposition 4 has any discriminatory effect, it would be *in favor of* interstate commercial activities undertaken by out-of-state actors.”(emphasis in original)); *Reynolds v. Buchholzer*, 87 F.3d 827, 829–30 (6th Cir. 1996).

<sup>140</sup> See CAL. CONST. art II, § 10(c) (“The Legislature may amend or repeal an initiative statute by another statute that becomes effective only when approved by the electors . . .”).

generally comparable in their impact to the embargo on imports.”<sup>141</sup> California “has a legitimate interest in guarding against imperfectly understood [health] risks, despite the possibility that they may ultimately prove to be negligible” and cannot be expected to “sit idly by and wait . . . until the scientific community agrees on what [ ] organisms are or are not dangerous before it acts to avoid such consequences.”<sup>142</sup> Therefore, even if the Court were to conclude AB 1437—because of its structuring or the legislative record—was protectionist, it should recognize it as falling within the bounds of an acceptable exception because its effects are not discriminatory. In the absence of discriminatory effect or intent, the *Pike* analysis is inapplicable in these cases.<sup>143</sup> As the ordinances in question neither burden nor discriminate against interstate commerce, they receive rational basis review. The Court should be cognizant of its admonition in *United Haulers* to “not seek to reclaim [a *Lochner*-esque] ground for judicial supremacy under the banner of the dormant Commerce Clause” and reject the plaintiffs’ “invitations to rigorously scrutinize [this] legislation passed under the auspices of the police power.”<sup>144</sup> The Court must be mindful to not let the doctrine become “a roving license for federal courts to decide what activities are appropriate for state and local government to undertake, and what activities must be the province of private market competition” as “the contrary approach . . . would lead to unprecedented and unbounded interference by the . . . courts with state and local government.”<sup>145</sup>

In this diversified and international market, the clear majority of police power exercises are liable to implicate interstate commerce. However, in the absence of discrimination, the burden of statute borne of a legitimate public purpose “is one which the Constitution permits because it is an inseparable incident of the exercise of a legislative authority, which, under the Constitution, has been left to the states.”<sup>146</sup> If the ordinances seek to prevent cruelty to animals occurring in the course of trade, they cannot be said to lack a rational basis.<sup>147</sup> That AB 1437 “does not protect the welfare of any animal in California” is irrelevant; the belief by the state legislature that eliminating a portion of the market for so-confined eggs will lead to better treatment is legitimate

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<sup>141</sup> See Regan, *supra* note 13, at 1270.

<sup>142</sup> *Maine v. Taylor*, 477 U.S. 131, 148 (1986) (discussing a Maine statute that prohibited the import of bait fishing).

<sup>143</sup> See *supra* notes 32–33 and accompanying text.

<sup>144</sup> *United Haulers Ass’n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 347 (2007).

<sup>145</sup> *Id.* at 343.

<sup>146</sup> *S.C. St. Highway Dep’t v. Barnwell Bros.*, 303 U.S. 177, 189 (1938).

<sup>147</sup> See *Cavel Int’l. v. Madigan*, 500 F.3d 551, 559 (7th Cir. 2007).

purpose enough.<sup>148</sup> The California and Massachusetts statutes are “demonstrably justified by a valid factor unrelated to economic protectionism.”<sup>149</sup> It has been more than three decades<sup>150</sup> since the Court invalidated a statute under the “permissive” balancing test<sup>151</sup> and should not start here, especially where the legitimate public interest, putative or otherwise, is of such great weight. The Solicitor General suggests that additional inquiry is necessary to properly perform *Pike*, but where statutes do not have a discriminatory effect, the *Pike* analysis is inapplicable;<sup>152</sup> the confinement statutes do not regulate on the basis of location, do not favor in-state interests over out-of-state interests and neither burden nor discriminate against interstate commerce and therefore should only be reviewed under rational basis which they easily surpass. The dormant Commerce Clause is simply not implicated when the burdens of a regulation are borne equally by in-state and out-of-state interests.<sup>153</sup>

Extraterritoriality, if applied even when the challenged statute does not implement protectionist discrimination, is wholly divorced from the purpose of the dormant Commerce Clause,<sup>154</sup> and, absent some limiting principle, poses a broad threat to a state’s authority to regulate conduct with direct effects within its bounds.<sup>155</sup> This over-inclusivity may indeed do damage to the principles animating the dormant Commerce Clause by striking down laws facilitating interstate commerce.<sup>156</sup> Unlike the pre-1989 laws struck down by the Court under the extraterritoriality doctrine, these laws do not, either by their terms or effect, directly regulate the sale of covered animal products in other states or prevent any other state from regulating the same production methods

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<sup>148</sup> See Motion For Leave To File Bill of Complaint, *supra* note 105, at 20; see also *Empacadora De Carnes de Fresnillo v. Curry*, 476 F.3d 326, 335–37 (5th Cir. 2007).

<sup>149</sup> *Town of Southold v. Town of E. Hampton*, 477 F.3d 38, 47 (2d Cir. 2007) (citing *Wyoming v. Oklahoma*, 502 U.S. 437, 454 (1992)).

<sup>150</sup> See *Edgar v. MITE Corp.*, 457 U.S. 624, 643–46 (1982).

<sup>151</sup> *United Haulers Ass’n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 347 (2007).

<sup>152</sup> See *supra* note 32–33 and accompanying text.

<sup>153</sup> See *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 126 (1978) (finding that the prohibition on operation of retail service stations did not create any barrier to interstate interests and therefore did not violate the dormant Commerce Clause).

<sup>154</sup> See *supra* note 58 and accompanying text.

<sup>155</sup> See *Energy & Env’t Legal Inst. v. Epel*, 793 F.3d 1169, 1175 (10th Cir. 2015) (“[I]f any state regulation that ‘control[s] . . . conduct’ out of state is *per se* unconstitutional, wouldn’t we have to strike down state health and safety regulations that require out-of-state manufacturers to alter their designs or labels?” (internal citation omitted)).

<sup>156</sup> See *Am. Beverage Ass’n v. Snyder*, 735 F.3d 362, 378 (6th Cir. 2013) (Sutton, J., concurring) (“Even a hypothetical state law that *facilitated* interstate commerce—say, an Ohio law that gave tax credits to automobile companies that keep open the production lines of their factories in Michigan and elsewhere—would be invalid if it had extraterritorial ‘practical effect[s].’” (quoting *Healy v. Beer Inst.*, 491 U.S. 326, 336 (1989))).

differently in their own jurisdiction. The simultaneous co-existence of the statutes challenged in these suits undermines any claim that each statute disrupts a national scheme. While evolving production standards may raise the specter of conflicting regimes, it is not a court's place to assume hypotheticals.<sup>157</sup> While the passage of price affirmation statutes in every state would result in "competing and interlocking local economic regulation,"<sup>158</sup> passage of confinement standards would result in national uniformity. To the extent one regime remains more restrictive than the others, it is up to each interstate market participant to determine for itself whether to comply with the most stringent and therefore continue to serve all states or narrow the jurisdictions in which they participate.<sup>159</sup> While out-of-state egg and hog farmers may choose to alter their production methods with regard to products for sale in other states—transactions in which California and Massachusetts have no interest—to avoid the costs of two distinct systems or spread the costs more broadly, nothing in either statute requires such meaning that such impacts are not "inescapable."<sup>160</sup>

It is incumbent on the Court to "surrende[r] former views"<sup>161</sup> of "heightened . . . *stare decisis* in the dormant Commerce Clause context"<sup>162</sup> "to a better considered position"<sup>163</sup> and recognize the dormancy of the presently conceived dormant Commerce Clause tests. Only by narrowing them to more closely reflect the interconnected realities of the present global economy will they do justice to the competing goals of federalism: state sovereignty and the equality of state law.<sup>164</sup>

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<sup>157</sup> See Regan, *supra* note 13, at 1148.

<sup>158</sup> Healy v. Beer Inst., 491 U.S. 326, 336 (1989).

<sup>159</sup> See *S. Pac. Co. v. Arizona*, 325 U.S. 761, 773, 795 (1945) (invalidating state train length law and noting that the alternative to breaking up trains at state borders "is for the carrier to conform to the lowest train limit restriction of any of the states through which its trains pass, whose laws thus control the carriers' operations both within and without the regulating state"); Donald H. Regan, *Siamese Essays: (I) CTS Corp. v. Dynamics Corp. of America and Dormant Commerce Clause Doctrine; (II) Extraterritorial State Legislation*, 85 MICH. L. REV. 1865, 1881 (1987) ("The commercial enterprise that chooses to operate in more than one state must simply be prepared to confirm its various local operations to more than one set of laws. The Constitution does not give an enterprise any special privileges just because it happens to operate across state lines.").

<sup>160</sup> See *supra* note 56 and accompanying text.

<sup>161</sup> *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080, 2100 (2018) (Thomas, J., concurring) (quoting *McGrath v. Kristensen*, 340 U.S. 162, 178 (1950) (Jackson, J., concurring)).

<sup>162</sup> *Id.* at 2102 (Roberts, C.J., dissenting).

<sup>163</sup> *Id.* at 2100 (Thomas, J., concurring) (quoting *McGrath v. Kristensen*, 340 U.S. 162, 178 (1950) (Jackson, J., concurring)).

<sup>164</sup> See Schmitt, *supra* note 46, at 426.





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