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State Taxation
Of Natural Resource
Extraction and the Commerce
Clause: Federalism's Modern Frontier

SINCE the oil embargo of 1973, the international price of energy has escalated dramatically, and a political and economic struggle has developed in the United States over how to divide the profits generated by spiraling energy prices. Producers, arguing the need for incentives and capital to develop new energy sources, have sought to increase the after-tax price of domestic energy. The government, arguing that "windfall" energy profits should be spent in the public interest, has levied or sought to levy higher taxes on energy. Consumers, arguing against the burdensome and disruptive effects of higher energy costs, have sought to lower or perpetuate current costs by supporting a variety of programs, including price regulation, innovative lifeline and inverted rate structures, and the installation of mandatory energy-conservation devices on cars, homes, and other energy-intensive consumer goods. Within this maelstrom of conflicting interests, one issue that raises a particularly significant problem of federalism is state taxation of natural resource extraction.

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For many years, most western states have taxed the extraction of natural resources. In the burst of energy development since 1973, many of these states focused attention on the form and level of resource taxation.¹ The result has been either new taxes or higher tax rates. A few examples are an increased tax rate on the severance of uranium in New Mexico,² a new resource severance tax in Colorado,³ a substantially increased tax rate on coal in Montana,⁴ and even a per kilowatt tax on the generation of electricity in New Mexico.⁵

The rest of the nation frequently views these tax developments as ill-disguised attempts by the resource-rich states to carve out larger shares of the profits derived from resource extraction. These larger shares are said to be unrelated to the costs the states incur from stepped-up mining.⁶ The resource-producing states counter that mining depletes their physical wealth, imposes undesirable consequences on portions of their populations, and may foreclose other developmental alternatives. These states argue that natural resource taxation is an appropriate way for them to obtain just compensation for the losses that result from the extraction and removal of natural resources.

The federal-state conflict over resource taxation is an ever-escalating one. The more the nation moves away from dependence on foreign sources of oil, the more it intensifies its inward search for resources. This search turns inevitably to the nonindustrialized, resource-rich western states. The western states, in turn, raise their tax rates to cover the higher externality costs associated with an accelerated rate of resource extraction and to prepare for the day when the resources will be exhausted. Since the resource-producing states pass the increased severance taxes on to the utilities and ultimately to consumers in sister states, the resource-dependent states cry "little OPEC." The resource-producing states respond with cries of "neocolonial exploitation." Although the extreme positions represented by these epithets can be re-

¹ The term *resource taxation*, as used in this Article, includes the full panoply of variously denominated state taxes levied on the severance or processing of natural resources within the taxing state. *E.g.*, N.M. STAT. ANN. § 7-25-4 (1978) (resources tax); N.M. STAT. ANN. § 7-25-5 (1978) (processors tax); N.M. STAT. ANN. § 7-25-6 (1978) (service tax); N.M. STAT. ANN. § 7-26-1 (1978) (severance tax). This Article focuses on state taxation of the severance of natural resources.

² N.M. STAT. ANN. § 7-26-7 (1978).

³ COLO. REV. STAT. §§ 39-29-101 to -114 (Supp. 1978).

⁴ MONT. CODE ANN. §§ 15-35-101 to -110 (1978).

⁵ N.M. STAT. ANN. §§ 7-18-1 to -6 (1978). The Supreme Court invalidated this statute in *Arizona Pub. Serv. Co. v. Snead*, 441 U.S. 141 (1979). *See generally* Note, *The Effect and Validity of State Taxation of Energy Resources*, 58 WASH. U. L.Q. 345, 347-57 (1980).

⁶ *See, e.g., Boom in Strip Mining: Windfall for Montana*, Washington Post, May 22, 1977, at 1, col. 1.

jected immediately, finding the actual dividing point between these extremes calls for very difficult decisionmaking under the federal commerce clause.

The resource taxation debate raises numerous ironies. The coal company that firmly cited *Carter v. Carter Coal Co.*⁷ for the proposition that the states have exclusive jurisdiction to regulate "local" coal mining operations must try to forget that proposition when it attacks a state severance tax on federal commerce clause grounds. The civil-rights-advocate-turned-environmentalist, who scoffed at southern "states' rights" and applauded *Katzenbach v. McClung*,⁸ must choke on Ollie's Barbeque sauce when he invokes state sovereignty to support a state severance tax enacted for environmental purposes. Likewise, the eastern liberal critic of the laissez faire economics of the pre-New Deal Court must now use that same Court's so-called free trade economics when she attacks western state laws that raise the cost of energy in the East.

These shifts in ideological positions illustrate just how difficult the federalism questions raised by modern resource development can be. For example, does the existence of a state line around a natural resource entitle the state to plan its future around the revenues that can be generated from the resource? While a ghost town may represent the ultimate in economic efficiency (when the resource is exhausted, the population shifts to another location where there is sufficient demand for employment), will our federal system tolerate ghost states?

The decisions of the Supreme Court help to focus these issues. In the view of Justice Frankfurter: "The interpenetrations of modern society have not wiped out state lines. It is not for us to make inroads upon our federal system either by indifference to its maintenance or excessive regard for the unifying forces of modern technology."⁹ The words of Justice Jackson must also be reckoned with.

Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his exports, and no foreign state will by customs duties or regulations exclude them.¹⁰

The current debate over increased resource taxation tests these most fundamental, if divergent, views of our federal union. It is clear that states have the power to tax extractive activities as well as other industrial and manufacturing processes that occur within their borders.¹¹ If,

⁷ 298 U.S. 238 (1936).

⁸ 379 U.S. 294 (1964).

⁹ *Polish Nat'l Alliance v. NLRB*, 322 U.S. 643, 650 (1944).

¹⁰ *H.P. Hood & Sons v. Du Mond*, 336 U.S. 525, 539 (1949).

¹¹ See text accompanying notes 57-67 *infra*.

however, a state exercises that power in a fashion that virtually prohibits the flow of extracted resources to out-of-state markets,¹² the state tax will violate the constitutional prohibition against unreasonable state interference with interstate commerce.¹³ The current challenge to Montana's coal severance tax in *Commonwealth Edison Co. v. State*¹⁴ frames the issue well. Out-of-state companies have challenged a tenfold increase in the Montana tax, the highest severance tax in the nation.¹⁵ Resolution of *Commonwealth Edison* by the United States Supreme Court will require at least a tentative striking of the commerce clause balance between state interests in resource taxation and the federal interest in the free flow of commerce.

This Article explores the modern commerce clause challenge to state taxation of natural resource extraction. After briefly tracing the historical development of the commerce clause, it turns to the early resource taxation cases, which established that the extraction of natural resources precedes commerce and is therefore shielded from commerce clause scrutiny. Next, it discusses three categories of modern commerce clause cases: state regulation cases, resource isolation cases, and state taxation cases. The Article then proceeds to demonstrate that (1) modern commerce clause developments have undercut the severance-precedes-commerce formula of the old resource taxation cases, rendering state severance taxes vulnerable to commerce clause scrutiny, and (2) the modern test for the constitutionality of state severance taxes will require an inquiry into the amount of and reasons for the particular tax. Finally, the Article discusses the specter of congressional preemption that now looms in the field of resource taxation, an area traditionally left to the exclusive control of state authority.

I

THE HISTORICAL BACKGROUND

Article I, section 8 of the United States Constitution enumerates the powers of Congress, one of which is the power "to regulate Commerce with foreign Nations, and among the several States, and with the

¹² See text accompanying notes 123-47 *infra*.

¹³ U.S. CONST. art. I, § 8, cl. 3; see text accompanying notes 16-25 *infra*.

¹⁴ 37 Mont. St. Rep. 1192, 615 P.2d 847, *prob. juris. noted*, 101 S. Ct. 607 (1980) (No. 80-581). The Montana Supreme Court upheld a dismissal of the out-of-state companies' complaints for failure to state a cause of action. It held that the tax was not levied on "an interstate activity" and therefore did not violate the commerce clause. *Id.* at 1201, 615 P.2d at 854. See generally Note, *The Increasing Conflict Between State Coal Severance Taxation and Federal Energy Policy*, 57 TEX. L. REV. 675 (1979).

¹⁵ The tax is at approximately 30% of value. MONT. CODE ANN. § 15-35-103 (1978).

Indian Tribes.”¹⁶ The explicit congressional power “to regulate Commerce . . . among the several States,” together with the negative implication that states may not invade that province,¹⁷ sparks the debate in commerce clause disputes. The debate always requires a resolution that inherently affects the balance between state and federal power. Indeed, the history of commerce clause adjudication is a history of the search for that balance of federal-state power that best serves the society’s needs at a particular time, with the recognition that those needs continually change and become increasingly complex. The historical origin of the clause itself provides only a small piece of the information necessary to understand how the clause applies to the complex political and economic disputes that characterize the modern cases. However, any attempt to suggest possible outcomes in commerce clause challenges must necessarily begin with a review of the provision’s origins.

The foremost problem of the federal union under the Articles of Confederation may have been its inability to tax.¹⁸ The failure of the Confederation may also be attributed, however, to the absence of national regulatory power over commerce, and to the resulting commercial “interstate brawls.”¹⁹ Trade barriers and acts of economic retribution among the states became so prevalent that in 1786 the Virginia Assembly felt compelled to propose what became the Annapolis Convention “to take into consideration the trade of the United States [and] to consider how far a uniform system in their commercial regulations may be necessary to their common interest and their permanent harmony.”²⁰ Although only five states sent representatives and nothing

¹⁶ U.S. CONST. art. I, § 8, cl. 3. In a case of first impression, the Tenth Circuit recently held that the commerce clause limits the powers of Indian tribes as well as those of the states, and that “the standard to be used in applying [the Indian commerce] clause is whether a tribe’s tax legislation infringes upon the national interest in maintaining the free flow of interstate trade. . . . measured by the traditional analyses.” *Merrion v. Jicarilla Apache Tribe*, 617 F.2d 537, 545 (10th Cir.), cert. granted, 101 S. Ct. 71 (1980) (No. 80–11).

¹⁷ See generally L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* § 6–2 (1978).

¹⁸ A. KELLY & W. HARBISON, *THE AMERICAN CONSTITUTION: ITS ORIGINS AND DEVELOPMENT* 108 (3d ed. 1963); S. MORISON, *THE OXFORD HISTORY OF THE AMERICAN PEOPLE* 304 (1965).

¹⁹ “There were enough interstate brawls to cause great disquiet. The New York assembly in 1787 assessed heavy entrance and clearance fees on all vessels coming from or bound to New Jersey and Connecticut; New Jersey retaliated by taxing the lighthouse on Sandy Hook £30 a month.” S. MORISON, *supra* note 18, at 304. See generally Sholley, *The Negative Implication of the Commerce Clause*, 3 U. CHI. L. REV. 556 (1936); Stern, *The Commerce Clause and the National Economy, 1933–1946*, 59 HARV. L. REV. 645 (1946).

²⁰ Resolution of the General Assembly of Virginia, Proposing a Joint Meeting of Commissioners from the States to Consider and Recommend a Federal Plan for Regulating Commerce (Jan. 21, 1786), reprinted in GOVERNMENT PRINTING OFFICE, *DOCUMENTS ILLUSTRATIVE OF THE FORMATION OF THE UNION OF THE AMERICAN STATES* 38 (1927) [hereinafter cited as DOCUMENTS].

substantive resulted, the report of the Annapolis Convention was one catalyst for the Constitutional Convention of 1787.²¹ The records of the Constitutional Convention,²² the Federalist Papers,²³ and the histories of the period²⁴ all indicate that the framers of the Constitution sought to overcome interstate rivalries and parochial protection of local economic interests. It is this purpose that modern Supreme Court opinions continue to describe as the original intent of the commerce clause.²⁵

Because the framers clearly intended to free national commerce from the strictures of state protectionism when they gave Congress the power "[t]o regulate Commerce . . . among the several States,"²⁶ it is curious

²¹ It was . . . to secure freedom of trade, to break down the barriers to its free flow, that the Annapolis Convention was called, only to adjourn with a view to Philadelphia. Thus the generating source of the Constitution lay in the rising volume of restraints upon commerce which the Confederation could not check. These were the proximate cause of our national existence down to today.

W. RUTLEDGE, *A DECLARATION OF LEGAL FAITH* 25 (1947).

While the Annapolis Convention was primarily concerned with removing barriers to commerce, the participants clearly recognized that this problem was linked with other aspects of the federal system.

In this persuasion, your Commissioners submit an opinion, that the Idea of extending the powers of their Deputies, to other objects, than those of Commerce, which has been adopted by the State of New Jersey, was an improvement on the original plan, and will deserve to be incorporated into that of a future Convention; they are the more naturally led to this conclusion, as in the course of their reflections on the subject, they have been induced to think, that the power of regulating trade is of such comprehensive extent, and will enter so far into the general System of the federal government, that to give it efficacy, and to obviate questions and doubts concerning its precise nature and limits, may require a correspondent adjustment of other parts of the Federal System.

Proceedings of the Commissioners to Remedy Defects of the Federal Government, Annapolis, Maryland (Sept. 14, 1786), *reprinted in* DOCUMENTS, *supra* note 20, at 39, 41-42.

²² 2 M. FARRAND, *THE RECORDS OF THE FEDERAL CONVENTION OF 1787*, at 308 (rev. ed. 1937); 3 *id.* at 478, 547-48. *See generally* S. PADOVER, *TO SECURE THESE BLESSINGS* 215-19 (1962).

²³ *THE FEDERALIST* NOS. 7, 11-12 (A. Hamilton), 41-42 (J. Madison).

²⁴ 1 G. CURTIS, *HISTORY OF THE ORIGIN, FORMATION, AND ADOPTION OF THE CONSTITUTION OF THE UNITED STATES* 502 (1854); M. FARRAND, *THE FRAMING OF THE CONSTITUTION OF THE UNITED STATES* 5-10 (1913); 1 F. THORPE, *THE CONSTITUTIONAL HISTORY OF THE UNITED STATES* 266-75 (1901).

²⁵ *See, e.g.*, *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979); *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 151 (1978) (Blackmun, J., concurring in part and dissenting in part); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 807 (1976); *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 523 (1935).

²⁶ U.S. CONST. art. I, § 8, cl. 3. The purpose of the commerce clause is similar to that of the import-export clause, which provides: "No State shall, without the

that they did not expressly address state interference with interstate commerce.²⁷ The Convention, however, was pervaded by a fundamental division between delegates who advocated a strong central government and those committed to state sovereignty as the primary principle of union.²⁸ An attempt to fashion language on state interference with interstate commerce could easily have led to a breakup of the Convention. The need to skirt that issue in order to reach consensus on the Constitution as a whole²⁹ may be the best explanation for the silence in the commerce clause concerning the limitations on state power to regulate commerce.³⁰

Consent of Congress, lay any Imposts or Duties on Imports or Exports” U.S. CONST. art. I, § 10, cl. 2. The import-export clause was intended, among other purposes, to prevent seaboard states from discriminating against inland states by taxing overseas imports and exports. 3 M. FARRAND, *supra* note 22, at 328–29; *see* *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 285 (1976). This purpose of nondiscrimination is common to both clauses.

But unlike the commerce clause, the import-export clause is a limitation on state power, not an affirmative grant of power to Congress. *See* L. TRIBE, *supra* note 17, §§ 6–2, –21. It has been construed as an absolute prohibition of state taxation of imports and exports. *Richfield Oil Corp. v. State Bd. of Equalization*, 329 U.S. 69, 76 (1946). In modern import-export cases, however, the Court is moving towards a balancing approach similar to that used in the modern commerce clause cases. The Court in *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976), reconsidered the purposes of the clause, *id.* at 285–90, including the purpose of preserving harmony among the states by preventing discrimination by seaboard states against inland states. *Id.* at 285. It then concluded that a nondiscriminatory ad valorem property tax on imported goods did not frustrate those purposes. *Id.* at 293–94.

Expanding the analysis of *Michelin Tire*, the Court in *Department of Revenue v. Association of Wash. Stevedoring Cos.*, 435 U.S. 734 (1978), applied commerce clause analysis, specifically the four-pronged test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977); *see* text accompanying notes 163–65 *infra*, to a tax on imports and exports. 435 U.S. at 761. Two years later, in *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 449–50 n.14 (1979), the Court elaborated on the similar purposes of the two clauses and again stated that under the import-export clause, a state tax on imports and exports must satisfy the same test for nondiscrimination as that required under the commerce clause.

²⁷ It has been suggested that the framers may have believed that the privileges and immunities clause, U.S. CONST. art. IV, § 2, was a sufficient limitation on state parochialism. L. TRIBE, *supra* note 17, § 6–2.

²⁸ *See generally* A. KELLY & W. HARBISON, *supra* note 18, at 114–47.

²⁹ As Alfred North Whitehead remarked: “The [framers] had an uncommonly clear grasp of the general ideas that they wanted put in here, then left the working out of the details to later interpreters” *THE DIALOGUES OF ALFRED NORTH WHITEHEAD* 204 (L. Price ed. 1954).

³⁰ An early commerce clause scholar suggests that the framers knew they could not grasp all the implications of the grant of the commerce power; therefore, they were unwilling to impose a categorical limitation on state action, preferring to leave such limitations to a fair application of the congressional power. F. RIBBLE, *STATE AND NATIONAL POWER OVER COMMERCE* 30 (1937).

Justice Jackson read the commerce clause silence as placing an affirmative duty

In any case, the framers' silence soon gave way to the strong federalist declarations of Chief Justice Marshall in *Gibbons v. Ogden*.³¹ In striking down a steamboat license monopoly granted by the New York legislature, the chief justice found that the state charter conflicted with a federal coastal licensing law. The federal licensing law was upheld as a valid exercise of the commerce power. Chief Justice Marshall then concluded that the conflicting state license violated the supremacy clause.³² The decision established the foundation for the theory of the exclusivity of federal power over commerce.³³

on the Court to promote the economic best interest of the country. "[E]ven more than by interpretation of its written word, this Court has advanced the solidarity and prosperity of this Nation by the meaning it has given to these great silences of the Constitution." *H.P. Hood & Sons v. Du Mond*, 336 U.S. 525, 535 (1949). It is not clear, however, that the commerce clause must be read as embracing a constitutionally compelled doctrine of national free trade. *See* note 33 *infra*.

³¹ 22 U.S. (9 Wheat.) 1 (1824).

³² *Id.* at 221.

³³ Chief Justice Marshall's opinion was not without ambiguity concerning whether the commerce power was exclusively federal.

The acknowledged power of a State to regulate its police, its domestic trade, and to govern its own citizens, may enable it to legislate on this subject, to a considerable extent

. . . .

Since, however, in exercising the power of regulating their own purely internal affairs, whether of trading or police, the States may sometimes enact laws, the validity of which depends on their interfering with, and being contrary to, an act of Congress passed in pursuance of the constitution, the Court will enter upon the inquiry, whether the laws of New York . . . have . . . come into collision with an act of Congress Should this collision exist, it will be immaterial whether those laws were passed in virtue of a concurrent power [to regulate commerce] or, in virtue of a power to regulate their domestic trade and police.

Id. at 208–10. Professor (later Justice) Frankfurter attributed the confusion in the Marshall opinion to the chief justice's desire to move cautiously in cementing his federalist doctrine.

Marshall's use of the commerce clause greatly furthered the idea that though we are a federation of states we are also a nation, and gave momentum to the doctrine that state authority must be subject to such limitations as the Court finds it necessary to apply for the protection of the national community.

F. FRANKFURTER, *THE COMMERCE CLAUSE UNDER MARSHALL, TANEY AND WAITE* 18–19 (W. Mendelson ed. 1973).

The ambivalence remains over whether the negative implication of the commerce clause is principally a device that helps to allocate the balance of state and federal power or whether it embodies the principle of national free trade. Unresolved by Chief Justice Marshall, this debate was perhaps most classically framed by Justices Frankfurter and Jackson. *See* text accompanying notes 9–10 *supra*. Not surprisingly, this same debate sharply divides the present Court. *Compare* *Reeves, Inc. v. Stake*, 447 U.S. 429, 438 (1980) (5–4 decision) (Blackmun, J.) ("Restraint in this area is also counseled by considerations of state sovereign-

If, as has always been understood, the sovereignty of Congress, though limited to specified objects, is plenary as to those objects, the power over commerce with foreign nations, and among the several States, is vested in Congress as absolutely as it would be in a single government, having in its constitution the same restrictions on the exercise of the power as are found in the constitution of the United States.³⁴

Owing perhaps to the natural law tradition underlying the early development of American constitutional law,³⁵ post-*Gibbons* commerce clause adjudication was marked by repeated but unsuccessful attempts to discover fundamental principles that could rationally and fairly be applied to all state regulations affecting interstate commerce. One such attempt was *Brown v. Maryland*.³⁶ *Brown* held that the commerce clause precluded Maryland from licensing wholesalers of imported goods when those goods remained in their original packages and still belonged to the importer.³⁷ Chief Justice Marshall, speaking for the Court, attempted to set out a principled distinction. "The power to direct the removal of gunpowder is a branch of the police power, which unquestionably remains, and ought to remain, with the States."³⁸ Numerous early commerce clause opinions seized on Marshall's distinction between regulations of interstate commerce and legitimate exercises of the states' "police power."³⁹

ty [and] the role of each State 'as guardian and trustee for its people' . . ."), *with id.* at 443 (Powell, J., dissenting) ("[T]he Commerce Clause long has been recognized as a limitation on [state] sovereignty, consciously designed to maintain a national market and defeat economic provincialism.").

³⁴ 22 U.S. (9 Wheat.) at 197. In a concurring opinion, Justice Johnson came to the issue more directly. He would have held that, irrespective of the federal law, the New York license was invalid as an invasion of the power left exclusively to Congress. "The inferences, to be correctly drawn, from this whole article, appear to me to be altogether in favour of the exclusive grants to Congress of power over commerce . . ." *Id.* at 236.

³⁵ See F. RIBBLE, *supra* note 30, at 8-19. See generally Corwin, *The "Higher Law" Background of American Constitutional Law*, 42 HARV. L. REV. 149 (1928); Harper, *Natural Law in American Constitutional Theory*, 26 MICH. L. REV. 62 (1927).

³⁶ 25 U.S. (12 Wheat.) 262 (1827).

³⁷ *Id.* at 267. The doctrine that precluded states from licensing or taxing foreign imports left in their original packages became known as the "original package" doctrine. It was weakened by later cases holding that when the imports are part of an inventory used to meet daily manufacturing needs, they become subject to state taxation, even though still in their original packages. *E.g.*, *Youngstown Sheet & Tube Co. v. Bowers*, 358 U.S. 534 (1959). The Supreme Court expressly disavowed the original package doctrine in *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 282-83 (1976).

³⁸ 25 U.S. (12 Wheat.) at 269.

³⁹ L. TRIBE, *supra* note 17, § 6-3, at 323; see, e.g., *Mayor of New York v. Miln*, 36 U.S. (11 Pet.) 102 (1837) (state requirement that masters of out-of-state

*Cooley v. Board of Wardens*⁴⁰ was the next commerce clause milestone. The Court, in an opinion authored by Justice Curtis,⁴¹ upheld a local requirement that interstate ships engage local pilots when entering and leaving the port of Philadelphia. The Court drew a distinction between those "subjects . . . imperatively demanding a single uniform rule" and those "as imperatively demanding that diversity, which alone can meet . . . local necessities."⁴² In the Court's view, the pilot regulation fell in the latter category and therefore passed commerce clause muster. In the following decades, the Court employed the *Cooley* doctrine to allow states to regulate aspects of commerce that were "local" in nature, while leaving to Congress the regulation of "national" aspects of commerce that required uniform rules.⁴³

The distinction between "national" and "local" subjects began to give way in the late nineteenth century, just as the distinction between "regulation of commerce" and "police power" previously had proved inadequate to resolve interstate commerce disputes. The development of more sophisticated commercial relationships required the Court to look beyond the *subject* of a state regulation to examine the *effect* of the regulation on the flow of commerce.⁴⁴ This focus on the regulation's impact on commerce led to the development of still another rubric for commerce clause analysis, which permitted state regulations to burden

vessels supply passenger lists was not a regulation of commerce but an exercise of police power). It has also been suggested that Marshall's opinion in *Wilson v. Black Bird Creek Marsh Co.*, 27 U.S. (2 Pet.) 245 (1829) (upholding Delaware's right to drain a marshy portion of a potential interstate waterway), implies that the Delaware statute fell "outside the ban of the 'dormant' commerce clause, because it [was] not a regulation of commerce, but of 'police.'" F. FRANKFURTER, *supra* note 33, at 29.

It should be understood that this commerce clause test was applied in an era when economic relationships had not yet become so complex that a piece of legislation could have the effect of regulating commerce even though its purpose was clearly "police" in nature. *Id.* at 30.

⁴⁰ 53 U.S. (12 How.) 299 (1851).

⁴¹ Chief Justice Taney, a member of the *Cooley* majority and Marshall's successor in 1836, advocated a different approach to the commerce clause than his predecessor. Taney believed that the commerce clause did not itself limit the exercise of state power. He saw the clause only as a grant of authority to Congress. In his view, the Court's role was to overrule state statutes only when necessitated by a direct conflict with an act of Congress. F. FRANKFURTER, *supra* note 33, at 50-51; see *License Cases*, 46 U.S. (5 How.) 504, 579 (1847).

⁴² 53 U.S. (12 How.) at 319.

⁴³ In *Wabash, St. L. & Pac. Ry. v. Illinois*, 118 U.S. 557 (1886), the Court struck down state regulation of railroad rates for interstate goods, even though there was no conflicting federal law. Fearing that the "cumulative burden" of such rates enacted by several states would be too disruptive of commerce (not unlike the state trade barriers of the Confederation, see note 19 *supra*), the Court decided that the area required national uniformity.

⁴⁴ L. TRIBE, *supra* note 17, § 6-4, at 325.

commerce “only indirectly, incidentally, and remotely.”⁴⁵ State regulations deemed so substantial as to constitute “direct” burdens on interstate commerce were struck down.⁴⁶

Each of these three successive tests, which evolved during the first century of commerce clause litigation,⁴⁷ has been criticized as “overly conclusory and misleadingly precise”⁴⁸ because it masked “the analysis underlying the decisions in which [it] played a role.”⁴⁹ Yet these tests remain important in modern commerce clause litigation both because they embody fundamental principles that still apply⁵⁰ and because the

⁴⁵ *Smith v. Alabama*, 124 U.S. 465, 482 (1888). In the most famous of the Grange Cases, *Munn v. Illinois*, 94 U.S. 113 (1876), which upheld state regulation of grain elevators, the Court applied the *Cooley* doctrine with overtones of the direct-versus-indirect formula. “[U]ntil Congress acts in reference to their interstate relations, the State may exercise all the powers of government over them, even though in so doing it may indirectly operate upon commerce outside its immediate jurisdiction.” *Id.* at 135.

⁴⁶ *E.g.*, *Seaboard Air Line Ry. v. Blackwell*, 244 U.S. 310 (1917).

⁴⁷ The foregoing discussion has focused on the Court’s attempts to define the permissible scope of state regulation during the century after *Gibbons*. Overlapping this doctrinal development was a general decline in the federal commerce power during the early twentieth century. Until the New Deal shift in the Court in 1937, the Court imposed its view of laissez faire economics to preclude federal legislation aimed at solving various social and economic problems caused by the American industrial revolution. *See* F. FRANKFURTER, *supra* note 33, at 115–17. One of the Court’s rationalizations for its refusal to extend congressional power was that certain aspects of production precede the flow of goods in commerce. *See, e.g.*, *United States v. E. C. Knight Co.*, 156 U.S. 1 (1895) (manufacturing is not commerce). It was during this period that the Court decided that the act of severing resources is not commerce. *See* text accompanying notes 52–62 *infra*. Because the narrow judicial view of the federal commerce power that prevailed during this period has been thoroughly repudiated by the post-1937 Court, those early severance tax cases are of questionable validity. *See* text accompanying notes 215–32 *infra*.

⁴⁸ L. TRIBE, *supra* note 17, § 6–5, at 326.

⁴⁹ *Id.* § 6–4, at 324.

⁵⁰ For example, the cumulative burden principle applied in modern state taxation cases clearly has its roots in the *Cooley* distinction between local subjects and subjects requiring national uniformity. This principle recognizes that when several states impose the same tax on an interstate business, the resulting cumulative burdens may prohibit a state tax that, viewed in isolation, does not unduly burden commerce. *E.g.*, *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 255–56 (1938).

Similarly, the modern resource isolation cases stem from the *Gibbons* principle that the federal commerce authority must be exclusive in order to prevent state trade barriers. *See, e.g.*, *Hughes v. Oklahoma*, 441 U.S. 322 (1979); *Philadelphia v. New Jersey*, 437 U.S. 617 (1978). Furthermore, the modern balancing test of *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), preserves the distinction between indirect and direct burdens on commerce. *Pike* includes as an element of its test an inquiry into whether a statute’s “effects on interstate commerce are only incidental.” *Id.* at 142.

modern Court will occasionally slip behind the comfortable obfuscation of one of these mechanical tests to reach a desired result.⁵¹

II

THE *Heisler* TRILOGY

Any attempt to apply the commerce clause to modern resource taxation problems must take into account that many of the cases directly concerning resource taxation were decided before the New Deal. During the 1920's, a period of judicially supported laissez faire economics,⁵² the Supreme Court decided a series of significant resource taxation cases known as the *Heisler* trilogy.⁵³ In all three cases, corporate taxpayers challenged state resource taxes on commerce clause grounds, arguing that the taxes both posed undue burdens on and discriminated against interstate commerce. In each case, the Supreme Court rejected these arguments. It concluded that the tax was applied to the act of severance or production, which preceded the flow of commerce and therefore was not subject to commerce clause constraints.⁵⁴

The issue in *Heisler v. Thomas Colliery Co.*⁵⁵ was framed by facts that track the modern problem. The challenged tax was levied on a type of anthracite coal found only in a few counties of Pennsylvania. The uniqueness of the coal put the state in a potentially monopolistic bargaining position.⁵⁶ Eighty percent of all the anthracite produced was shipped to states where the coal was a necessity because of local laws that prohibited the use of more prevalent coal of higher sulphur content.

⁵¹ The debate between the majority and the dissenting justice in *Exxon Corp. v. Governor of Md.*, 437 U.S. 117 (1978), is illustrative. In upholding a Maryland law that required oil producers and refiners to divest themselves of retail operations in the state, Justice Stevens, writing for the majority, reasoned: "The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination . . ." *Id.* at 126. In dissent, Justice Blackmun argued that the law was discriminatory. He pointed out that "the burden [was] *significant* [and fell] on the most numerous and effective group of out of state competitors." *Id.* at 148 (emphasis added). This debate is but one modern application of the old distinction between direct (Blackmun) and indirect (Stevens) burdens on commerce. It seems no less conclusory now than it did when first enunciated.

⁵² See note 47 *supra*.

⁵³ *Hope Natural Gas Co. v. Hall*, 274 U.S. 284 (1927); *Oliver Iron Mining Co. v. Lord*, 262 U.S. 172 (1923); *Heisler v. Thomas Colliery Co.*, 260 U.S. 245 (1922).

⁵⁴ "Mining is not interstate commerce, but, like manufacturing, is a local business subject to local regulation and taxation." *Oliver Iron Mining Co. v. Lord*, 262 U.S. 172, 178 (1923).

⁵⁵ 260 U.S. 245 (1922).

⁵⁶ The coal was taxed at only one and one-half percent of its value when prepared for market. *Id.* at 253.

These facts parallel the present demand for western coal and uranium.

The taxpayer in *Heisler* advanced the commerce clause argument that “a tax upon [anthracite coal] is levying a tribute upon the consumption of other States.”⁵⁷ The Court expressed concern, however, that if the mere fact that a product was destined for shipment out of state were held to place the product in interstate commerce, states would not be able to tax any commercial activities within their borders.⁵⁸ For this reason, it held that a tax levied when coal has been mined and is ready for shipment precedes the time at which the coal is “governed and protected by the national law of commercial regulation.”⁵⁹

Heisler was followed by *Oliver Iron Mining Co. v. Lord*,⁶⁰ which held that mining is not interstate commerce. In the third case in the trilogy, *Hope Natural Gas Co. v. Hall*,⁶¹ the Court treated as settled

⁵⁷ *Id.* at 258.

⁵⁸ If the possibility, or, indeed, certainty of exportation of a product or article from a State determines it to be in interstate commerce before the commencement of its movement from the State, it would seem to follow that it is in such commerce from the instant of its growth or production, and in the case of coals, as they lie in the ground. The result would be curious. It would nationalize all industries, it would nationalize and withdraw from state jurisdiction and deliver to federal commercial control the fruits of California and the South, the wheat of the West and its meats, the cotton of the South, the shoes of Massachusetts and the woolen industries of other States, at the very inception of their production or growth, that is, the fruits unpicked, the cotton and wheat un-gathered, hides and flesh of cattle yet “on the hoof,” wool yet unshorn, and coal yet unmined, because they are in varying percentages destined for and surely to be exported to States other than those of their production.

Id. at 259–60.

⁵⁹ *Id.* at 260–61 (quoting *Coe v. Errol*, 116 U.S. 517, 525 (1886)). *Coe* held that the commerce clause did not prohibit a New Hampshire town from taxing logs drawn down a New Hampshire river and stored in the town for later shipment to Maine. Like the Court in *Heisler*, the *Coe* Court could see no limit to the taxpayer’s commerce clause argument.

It seems to us untenable to hold that a crop or a herd is exempt from taxation merely because it is, by its owner, intended for exportation. If such were the rule in many States there would be nothing but the lands and real estate to bear the taxes. Some of the Western States produce very little except wheat and corn, most of which is intended for export; and so of cotton in the Southern States. Certainly, as long as these products are on the lands which produce them, they are part of the general property of the State. And so we think they continue to be until they have entered upon their final journey for leaving the State and going into another State.

116 U.S. at 527–28.

⁶⁰ 262 U.S. 172 (1923). Practically all the ore mined was shipped out of state. There was also clear continuity of movement out of the state once the ore was severed.

⁶¹ 274 U.S. 284 (1927). At issue was a West Virginia privilege tax on production of natural gas, measured by the value of the gas at the wellhead.

doctrine the principle that a privilege or occupation tax on the mining or production of resources does not violate the commerce clause. This early distinction between "local business" and "the flow of interstate commerce" has insulated state resource taxation from successful commerce clause challenge to the present day.⁶²

Later cases gave renewed support to the result of the *Heisler* trilogy. In *Michigan-Wisconsin Pipe Line Co. v. Calvert*,⁶³ the Court suggested in dictum that the commerce clause does not prevent states from taxing resource extraction. It went on to hold, however, that the state had delayed the incidence of the tax until production had ceased and transmission in commerce had begun, rendering the tax invalid.⁶⁴ In *Alaska v. Arctic Maid*,⁶⁵ the Court reaffirmed the distinction between taxes on local activities and taxes on the flow of commerce. It upheld Alaska's four percent tax on fish taken by out-of-state freezer ships for immediate transportation to out-of-state canneries. Harking back to the *Heisler* trilogy, the Court held that the event taxed was the local business of taking fish.⁶⁶ In 1969 the Court again relied on the notion that certain activities precede commerce when it sustained an Alabama tax on photographers who engage in the "local activity" of taking pictures in Alabama.⁶⁷

The *Heisler* trilogy, although not yet applied by the modern Court to a state severance tax, has been bolstered by the subsequent support of

⁶² For example, in *Utah Power & Light Co. v. Pfof*, 286 U.S. 165 (1932), the Court relied heavily on *Oliver Iron Mining Co.* and *Hope Natural Gas Co.* to conclude that the generation of electricity was sufficiently distinct from its transmission to justify a state tax on generation.

We are satisfied, upon a consideration of the whole case, that the process of generation is as essentially local as though electrical energy were a physical thing; and to that situation we must apply, as controlling, the general rule that commerce does not begin until manufacture is finished, and hence the commerce clause of the Constitution does not prevent the state from exercising exclusive control over the manufacture.

Id. at 181. See also *Coverdale v. Arkansas-Louisiana Pipe Line Co.*, 303 U.S. 604 (1938) (tax on production of mechanical power for interstate pipeline held a valid local privilege tax).

⁶³ 347 U.S. 157 (1954).

⁶⁴ *Id.* at 167-68. In so holding, the Court once more distinguished "processing" and "production" from "transmission in interstate commerce." *Id.* at 167.

⁶⁵ 366 U.S. 199 (1961).

⁶⁶ The *Oliver Iron* case is indeed a first cousin of the present case. Here, as there, the tax is an occupation tax. Here, as there, the market for the product obtained locally is interstate, the taking being a step in a process leading to an interstate market. In both the local product is promptly loaded for interstate shipment. But in each there is a preliminary local business being conducted—an occupation made up of a series of local activities which the State can constitutionally reach.

Id. at 204.

⁶⁷ *Dunbar-Stanley Studios, Inc. v. Alabama*, 393 U.S. 537, 541 (1969).

Michigan-Wisconsin Pipe Line, Arctic Maid, and numerous state court cases.⁶⁸ While the *Heisler* trilogy and its modern progeny appear to present a firm and fixed principle of commerce clause adjudication, the undercurrents of change are much in evidence. First, there has been a general shift by the Court away from formalistic commerce clause tests towards a balancing approach that allows for the accommodation of competing interests.⁶⁹ Second, the Court consistently has required state laws that effectively isolate natural resources from the national economy to meet a stricter commerce clause test than other state laws.⁷⁰ Finally, there has been an erosion of the doctrinal view that precluded states from fairly taxing the flow of commerce.⁷¹ All these trends sug-

⁶⁸ See, e.g., *Industrial Uranium Co. v. State Tax Comm'n*, 95 Ariz. 130, 387 P.2d 1013 (1963) (upholding Arizona's transaction privilege tax on the gross proceeds or gross income from mining); *California Co. v. State*, 141 Colo. 288, 348 P.2d 382 (1959) (graduated excise tax on gross income derived from the extraction or production of crude oil and natural gas located within the state); *Bel Oil Corp. v. Roland*, 242 La. 498, 137 So. 2d 308 (1962) (severance tax on natural gas); *Virginia Elec. & Power Co. v. Haden*, 200 S.E. 2d 848 (W. Va. 1973), *cert. denied*, 416 U.S. 916 (1974) (tax on the generation of electricity). In each of these cases, the state court applied the reasoning of the *Heisler* trilogy to uphold the challenged tax, characterizing it as a tax on a local business activity that preceded the flow of interstate commerce. This severance-precedes-commerce analysis also underlies the Montana Supreme Court's opinion in *Commonwealth Edison Co. v. State*, 37 Mont. St. Rep. 1192, 615 P.2d 847, *prob. juris. noted*, 101 S. Ct. 607 (1980) (No. 80-581). See note 14 and accompanying text *supra*.

The three most recent state supreme court decisions on resource taxation focus on discrimination against out-of-state consumers through disparate tax credits given to in-state taxpayers. *Arizona Pub. Serv. Co. v. O'Chesky*, 91 N.M. 485, 576 P.2d 291 (1978) (upholding New Mexico tax on the generation of electricity), *rev'd sub nom.* *Arizona Pub. Serv. Co. v. Snead*, 441 U.S. 141 (1979); *Post Oak Oil Co. v. Oklahoma Tax Comm'n*, 575 P.2d 964 (Okla. 1978) (upholding conservation excise tax on gas produced in Oklahoma); *Public Util. Dist. No. 2 v. State*, 82 Wash. 2d 232, 510 P.2d 206, *appeal dismissed*, 414 U.S. 1106 (1973) (upholding Washington tax on the generation of electricity).

In *Arizona Public Service*, the United States Supreme Court struck down the New Mexico electrical energy tax as discriminatory and in contravention of a federal statute. 441 U.S. at 146-50. This federal statute, however, was not in effect when the Washington Supreme Court upheld Washington's power generation tax against similar discrimination claims in *Public Utility District No. 2*. The Court in *Arizona Public Service* expressly refused to determine the validity of the Washington tax. *Id.* at 150 n.7.

In *Post Oak*, the Oklahoma conservation excise tax faced a similar discrimination challenge, as well as an argument that the tax unduly burdened commerce. To answer the latter argument, the Oklahoma Supreme Court resorted to an *Oliver Iron* solution. The court held that the tax was on the local act of severance and production and that it imposed only an incidental burden on interstate commerce. 575 P.2d at 968. For a commerce clause analysis of the Oklahoma tax, see Note, *supra* note 5, at 348, 353-54.

⁶⁹ See text accompanying notes 76-122 *infra*.

⁷⁰ See text accompanying notes 123-47 *infra*.

⁷¹ See text accompanying notes 148-214 *infra*.

gest that the *Heisler* trilogy's simple distinction between activities "in" commerce and those "out of" commerce will be insufficient to resolve modern severance taxation cases.

III

THE MODERN COMMERCE CLAUSE ANALYSIS

The modern commerce clause decisions⁷² recognize that the clause requires a complex "reconciliation of the conflicting claims of state and national power" that can only be accomplished through a careful "appraisal and accommodation of the competing demands of the state and national interests."⁷³ They also recognize that, in the absence of congressional action,⁷⁴ the Court is the final arbiter of these competing interests and, concomitantly, it is the Court that must intervene when necessary to carry out the framers' intent to protect our national economy.⁷⁵

This section of the Article explores three categories of commerce clause cases that illustrate the principles likely to govern modern severance taxation questions. The state regulation cases demonstrate the factors the Court considers when it balances state regulatory interests against burdens on interstate commerce. The resource isolation cases suggest that the balancing approach may give way to per se invalidity when the state statute smacks of trade barrierism. Finally, the balancing approach first developed in the state regulation cases is shown to have found its way into the modern state taxation cases and thus to have undercut the *Heisler* line of cases.

A. The State Regulation Cases

The modern commerce clause balancing test is most clearly articulated in *Pike v. Bruce Church, Inc.*⁷⁶

Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose is

⁷² The modern era of commerce clause adjudication began with the 1937 shift in the Court. See note 47 *supra*.

⁷³ *Southern Pac. Co. v. Arizona*, 325 U.S. 761, 768-69 (1945).

⁷⁴ For a discussion of the possibilities for congressional preemption of state severance taxes, see text accompanying notes 254-88 *infra*.

⁷⁵ See F. FRANKFURTER, *supra* note 33, at 21-22. Later, the then Justice Frankfurter wrote: "The task of scrutinizing is a task of drawing lines. This is the historic duty of the Court so long as Congress does not undertake to make specific arrangements between the National Government and the States in regard to revenues from interstate commerce." *Freeman v. Hewit*, 329 U.S. 249, 253-54 (1946).

⁷⁶ 397 U.S. 137 (1970).

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.⁷⁷

Pre-*Pike* decisions often failed to formulate a test, and post-*Pike* decisions invariably begin their analyses with the *Pike* formulation. Each of the commerce clause regulation cases in which the Court used a balancing approach can be explained by some or all of the components of the *Pike* test: (1) evenhandedness, (2) legitimacy of the local public interest, (3) burden imposed on commerce in relation to local benefit, and (4) least intrusive means.⁷⁸

1. *Evenhandedness*

The evenhandedness component of the *Pike* test focuses on whether the legislation discriminates against interstate commerce.⁷⁹ While the cases do not require absolute equality of treatment of interstate and intrastate commerce, if the Court finds discrimination,⁸⁰ it will scrutinize the state legislation more closely and require the state to offer greater justification for the statute.⁸¹ Indeed, in cases that involve

⁷⁷ *Id.* at 142 (citation omitted). *Pike* invalidated a state statute that required Arizona cantaloupes to be packed in the state. The Court suggested, however, that state regulations that affect public health or safety might be subjected to a lesser standard of scrutiny. *Id.* at 143–44.

⁷⁸ Most recently, the Court has restated the *Pike* test as a three-pronged test: Under [the] general rule we must inquire (1) whether the challenged statute regulates evenhandedly with only “incidental” effects on interstate commerce, or discriminates against interstate commerce either on its face or in practical effect; (2) whether the statute serves a legitimate local purpose; and if so, (3) whether alternative means could promote this local purpose as well without discriminating against interstate commerce.

Hughes v. Oklahoma, 441 U.S. 322, 336 (1979).

⁷⁹ Although *Pike* states the test for discrimination separately from that for burden, the two tests often employ the same balancing approach. This approach analyzes the state objective, the purpose behind that objective, and the means chosen to achieve the particular end. For a recent articulation of the discrimination and burden components of *Pike* as a single test, see note 78 *supra*.

⁸⁰ Theoretically, a finding of discrimination against interstate commerce may be overcome by the absence of less restrictive means to protect a legitimate state interest, but no decision fully applies that analysis. In fact, a finding of discrimination usually sounds the death knell of a state statute challenged on commerce clause grounds. When the Court upholds a statute, it often resorts to formalistic tests in order to avoid pronouncing the statute discriminatory. *See, e.g.*, *Exxon Corp. v. Governor of Md.*, 437 U.S. 117 (1978) (Maryland’s prohibition against oil producers or refiners operating retail service stations burdened commerce only incidentally; therefore it was not discriminatory).

⁸¹ The evenhandedness requirement of *Pike* parallels the nondiscrimination requirement of the privileges and immunities clause, U.S. CONST. art. IV, § 2.

facial discrimination similar to a trade barrier,⁸² the lack of evenhandedness triggers an almost per se rule of invalidity.⁸³ A facially discriminatory statute that encourages retaliation by sister states⁸⁴ or requires action by a sister state to make its application evenhanded⁸⁵ will also receive close scrutiny. Even when the statute is evenhanded on its face, the Court will examine the practical effect of the statutory scheme to determine whether it is discriminatory in operation. When the effect is clearly discriminatory and without substantial justification, the statute will fall.⁸⁶

2. *Legitimacy of the Local Public Interest*

As a legacy of the old distinction between "police power" and "regulation of commerce,"⁸⁷ the modern cases focus on the nature of the local interest protected. To the extent that these cases maintain the old distinction, they can be viewed as presenting a hierarchy of local interests.⁸⁸ The more legitimate the local interest, the less judicial scrutiny the Court seems to require.

At the bottom of the hierarchy, a state's attempts to regulate its

The privileges and immunities clause insures to citizens of each state the same rights of state citizenship held by citizens of any other state into which they venture. It prohibits a state from discriminating against nonresidents when "there is no substantial reason for the discrimination beyond the mere fact that they are citizens of other States." *Toomer v. Witsell*, 334 U.S. 385, 396 (1948); see *Hicklin v. Orbeck*, 437 U.S. 518 (1978). The Court has allowed preferential treatment of residents over nonresidents only when it is supported by a valid reason that bears a close relationship to the degree of discrimination. One example of a legitimate reason for preferential treatment is the protection of wildlife. *Baldwin v. Fish & Game Comm'n*, 436 U.S. 371 (1978).

⁸² The difficulty of overcoming clear and demonstrable discrimination is well illustrated by the milk regulation cases. See, e.g., *Polar Ice Cream & Creamery Co. v. Andrews*, 375 U.S. 361 (1964) (attempt to reserve local market for local milk held invalid discrimination against interstate commerce); *Dean Milk Co. v. City of Madison*, 340 U.S. 349 (1951) (invalidating a requirement that milk sold in the city be pasteurized within five miles of city); *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935) (striking down a prohibition against in-state resale of milk purchased outside the state at prices below state minimum).

⁸³ See text accompanying notes 123-47 *infra*.

⁸⁴ See, e.g., *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978); *Public Util. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927).

⁸⁵ See *Great Atl. & Pac. Tea Co. v. Cottrell*, 424 U.S. 366 (1976).

⁸⁶ E.g., *Hunt v. Washington State Apple Advertising Comm'n*, 432 U.S. 333 (1977) (North Carolina restriction on the labeling of apples shipped into state discriminated against the interstate sale of Washington apples).

Although one might also expect that a law discriminatory on its face but evenhanded in operation will pass constitutional muster, *Hughes v. Oklahoma*, 441 U.S. 322 (1979), suggests that this is not the case. "Such facial discrimination by itself may be a fatal defect, regardless of the State's purpose . . ." *Id.* at 337.

⁸⁷ See text accompanying notes 40-46 *supra*.

⁸⁸ See generally *L. TRIBE*, *supra* note 17, §§ 6-6 to -8, 6-12.

economic well-being border on per se illegitimacy.⁸⁹ If the purpose⁹⁰ or predominant effect⁹¹ of a regulation is to protect local markets from interstate competition, the regulation is clearly suspect. Somewhat higher in the hierarchy is a state's interest in the safety of its citizens. In the train and truck regulation cases, the Court gave safety regulations a strong presumption of validity when they conflicted with the commerce clause.⁹² At the top of the hierarchy, state regulation of public health receives the greatest deference from the Court. The quarantine cases, in which the Court upheld statutes prohibiting the importation of diseased cattle or decayed or noxious food,⁹³ are the clearest example of the Court's deference to state health regulations despite direct and substantial impacts on commerce.⁹⁴

As the interest protected by the regulation moves from the economic sphere towards public safety and health, it becomes more likely that the statute will withstand commerce clause attack. *Raymond Motor Transportation, Inc. v. Rice*⁹⁵ establishes, however, that the mere recitation of a health or safety purpose will not suffice; the regulation must actually further the interest asserted. In that case, the Court struck down a state-imposed truck-length limitation because the state had failed to produce evidence to counter the plaintiff's massive evidence that the law did not contribute to highway safety.⁹⁶ Furthermore, *City of Philadelphia v. New Jersey* shows that even when the state's health or safety aims are genuine, the statutory means selected to achieve the desired

⁸⁹ *But see* notes 98–102 and accompanying text *infra*.

⁹⁰ *See, e.g.,* *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935); *Foster-Fountain Packing Co. v. Haydel*, 278 U.S. 1 (1928).

⁹¹ *See, e.g.,* *Hunt v. Washington State Apple Advertising Comm'n*, 432 U.S. 333 (1977).

⁹² *See* *Brotherhood of Locomotive Firemen v. Chicago, R.I. & Pac. R.R.*, 393 U.S. 129 (1968); *South Carolina Highway Dep't v. Barnwell Bros.*, 303 U.S. 177 (1938).

⁹³ *Mintz v. Baldwin*, 289 U.S. 346 (1933) (unhealthy cattle); *Price v. Illinois*, 238 U.S. 446 (1915) (food preservative); *Asbell v. Kansas*, 209 U.S. 251 (1908) (unhealthy cattle); *Crossman v. Lurman*, 192 U.S. 189 (1904) (adulterated foods).

⁹⁴ Although these cases have been rationalized on the theory that the prohibited products were "not proper subjects of commerce," *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 525 (1935), they are more fairly understood as balancing cases in which the states' interest in prohibiting noxious products reasonably outweighed the interference with commerce. L. TRIBE, *supra* note 17, at 28 n.43 (Supp. 1979).

⁹⁵ 434 U.S. 429 (1978).

⁹⁶ The Court clearly understood that safety, like other legitimate state interests, must be weighed against interference with interstate commerce. *Id.* at 443. It has been suggested, however, that if safety justifications are supported by the factual record, "the Court will not second-guess legislative judgment about their importance in comparison with related burdens on interstate commerce." *Id.* at 449 (Blackmun, J., concurring); *see* notes 110–14 and accompanying text *infra*.

result may also be a factor to balance.⁹⁷

Finally, the mere fact that a regulation touches on economic matters will not automatically invalidate it. Conserving natural resources,⁹⁸ controlling agricultural production,⁹⁹ and maintaining environmental quality¹⁰⁰ all have been recognized as legitimate legislative purposes.¹⁰¹ Indeed, most recently, the Court has suggested in dictum that the legitimate purposes of state regulation may even include protecting the state's economic well-being; the state may legitimately ensure a steady supply of milk, create jobs, preserve its financial resources, or otherwise "protect its residents' pocketbooks."¹⁰²

Thus, although the modern Court sometimes has maintained the traditional economics-safety-health hierarchy of state interests, not all its decisions fit within this hierarchy. The Court has acknowledged that the complexities of modern state government require a broader range of legitimate state regulation than the traditional areas of safety and health. At the same time, however, it has recognized an expanding national interest in the free flow of commerce, against which the states' legitimate interests must be weighed.¹⁰³

3. *Burden on Commerce in Relation to Local Benefit*

The third component of the *Pike* test asks whether "the burden imposed on . . . commerce is clearly excessive in relation to the putative local benefits."¹⁰⁴ This balancing of state and federal interests has been

⁹⁷ See 437 U.S. 617, 625 (1978). "If reasonable nondiscriminatory alternatives, adequate to conserve legitimate local interests, are available," even unquestioned health concerns must give way. *Dean Milk Co. v. City of Madison*, 340 U.S. 349, 354 (1951).

⁹⁸ See *Cities Serv. Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179 (1950).

⁹⁹ See *Parker v. Brown*, 317 U.S. 341 (1943).

¹⁰⁰ See *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440 (1960).

¹⁰¹ In each of the cases cited in notes 98-99 *supra*, however, the Court engaged in substantial balancing of state and federal interests.

¹⁰² *City of Philadelphia v. New Jersey*, 437 U.S. 617, 626 (1978). The Court has also recognized that a state may legitimately control its retail gasoline market by requiring out-of-state producers to divest themselves of retail businesses within the state. *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 125 (1978). Furthermore, the state may enter the interstate market as a proprietary participant in commerce and avoid the commerce clause limitations that would apply to it in its regulatory and taxing capacity. *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980) (state as producer of cement may favor state residents); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976) (state may favor in-state dealers over out-of-state dealers when it purchases junk cars converted into scrap).

¹⁰³ See, e.g., text accompanying notes 110-14 *infra*.

¹⁰⁴ 397 U.S. at 142. *Pike* seems to suggest that the balancing of burden and local benefit will take place only if the statute's "effects on interstate commerce are . . . incidental." *Id.* This reversion to the old direct-versus-indirect formula, see notes 44-46 and accompanying text *supra*, plays little part in modern commerce clause analysis. As a practical matter, statutes found to withstand the *Pike*

a constant theme in commerce clause adjudication.¹⁰⁵ For example, in *Bibb v. Navajo Freight Lines, Inc.*,¹⁰⁶ the Court used a balancing approach to strike down an Illinois requirement that trucks have contour mudguards. Because contour mudguards were not measurably safer than the straight ones allowed in forty-five other states, the showing of added safety was insufficient to outweigh the burden on interstate commerce.¹⁰⁷ In *Southern Pacific Co. v. Arizona*,¹⁰⁸ marginal safety interests were similarly balanced against heavy burdens on commerce, resulting in the invalidation of Arizona's train-length limitation.¹⁰⁹

In contrast with *Bibb* and *Southern Pacific*, some Supreme Court decisions¹¹⁰ have suggested that health and safety considerations should not be balanced against mere economic loss; instead, the Court should defer to the state legislatures' weighing of these considerations against

balancing test are also found to have an incidental effect on commerce, *see, e.g.*, *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 126 (1978), and those that fail the test are found to have a substantial or direct effect on commerce. *See, e.g.*, *Hunt v. Washington State Apple Advertising Comm'n*, 432 U.S. 333 (1977).

¹⁰⁵ It has been suggested that the *Cooley* test is essentially a balancing of state and federal interests, although "conducted under the guise of 'classifying' the state interest" as local or national. L. TRIBE, *supra* note 17, § 6-12, at 341.

¹⁰⁶ 359 U.S. 520 (1959).

¹⁰⁷ The burden included the cost of installing the contour mudguards (\$30 or more per vehicle) as well as the delay caused by changing mudguards. *Id.* at 525, 527.

¹⁰⁸ 325 U.S. 761 (1945).

¹⁰⁹ The Arizona train-length limitation was deemed to afford "at most slight and dubious advantage, if any, over unregulated train lengths." *Id.* at 779. Against this were balanced the facts that (1) over 90% of the rail traffic affected was interstate, *id.* at 770; (2) the limitation was enforced in only two states, *id.* at 774; and (3) it would cost carriers about \$1,000,000 per year to comply. *Id.* at 772.

¹¹⁰ In *Brotherhood of Locomotive Firemen v. Chicago, R.I. & Pac. R.R.*, 393 U.S. 129 (1968), the Court invoked a traditional rational relationship test to uphold a statute requiring full crews on railroad lines within the state. In deferring to the state legislative judgment that public safety required full crews, the Court commented that "[i]t is difficult at best to say that financial losses should be balanced against the loss of lives and limbs of workers and people using the highways." *Id.* at 140.

Similarly, in *South Carolina Highway Dep't v. Barnwell Bros.*, 303 U.S. 177 (1938), the Court upheld a truck size and weight limitation, inquiring only sufficiently to assure itself that the regulation had some rational basis. The Court brushed aside the fact that approximately 90% of interstate trucks exceeded the limitation, noting that the regulation's coverage of intrastate as well as interstate carriers was "a safeguard against [its] abuse." *Id.* at 187.

According to Professor Tribe, the rationale underlying the safeguard-against-abuse notion in *Barnwell* is that nondiscriminatory regulations are less likely to offend the commerce clause "when the interests adversely affected have been adequately represented in the regulating state's own political process." L. TRIBE, *supra* note 17, § 6-5, at 327. *See also* *Southern Pac. Co. v. Arizona*, 325 U.S. 761, 767-68 n.2 (1945).

the attendant burdens on commerce.¹¹¹ The recent decision in *Raymond Motor Transportation, Inc. v. Rice*¹¹² rejected this view, however. While conceding that great deference was due to the state legislative judgments behind health and safety regulations, the Court in *Raymond Motor* ultimately accepted the balancing approach: “[W]e cannot accept the State’s contention that the inquiry under the Commerce Clause is ended without a weighing of the asserted safety purpose against the degree of interference with interstate commerce.”¹¹³ Thus, even when the state purpose is legitimate and proper deference is given to the legislative judgment, the Court will nevertheless weigh the competing federal interests.¹¹⁴

4. *Least Intrusive Means*

Even if a particular regulation furthers a legitimate local purpose, the *Pike* test will not permit it to burden commerce when the purpose “could be promoted as well with a lesser impact on interstate activities.”¹¹⁵ This least-intrusive-means requirement traditionally has been applied to state regulations that serve a legitimate state purpose but are discriminatory on their face or in effect.¹¹⁶ Even the most compelling and legitimate local purpose will not save a discriminatory regulation unless there are no “reasonable nondiscriminatory alternatives” available that are “adequate to conserve” the local interest.¹¹⁷ Thus, the

¹¹¹ Some lower courts have adopted this view. *See, e.g., American Can Co. v. Oregon Liquor Control Comm’n*, 15 Or. App. 618, 517 P.2d 691 (1973) (upholding the Oregon bottle deposit law).

¹¹² 434 U.S. 429 (1978).

¹¹³ *Id.* at 443. *But see id.* at 449 (Blackmun, J., concurring).

¹¹⁴ A further consideration under this prong of the *Pike* test is whether the challenged state regulation must actually burden interstate business or whether a potential for burden is sufficient to trigger invalidation. The early cases suggested that a potential for burden is sufficient, but those cases arose in a civil rights context. *See Morgan v. Virginia*, 328 U.S. 373 (1946); *Hall v. DeCuir*, 95 U.S. 485 (1878). Their use of a potential-for-conflict rationale to strike down state-imposed racial segregation on interstate trains before the rise of equal protection analysis may not be representative of solid commerce clause analysis. A more recent case has suggested that mere potential for conflict is not enough. *See Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440, 448 (1960).

¹¹⁵ 397 U.S. at 142. The Court first clearly articulated a least-intrusive-means test in *Dean Milk Co. v. City of Madison*, 340 U.S. 349, 354 (1951). The *Pike* formula incorporated essentially the same test.

¹¹⁶ *See Hunt v. Washington State Apple Advertising Comm’n*, 432 U.S. 333 (1977); *Dean Milk Co. v. City of Madison*, 340 U.S. 349, 354 (1951). In *Hughes v. Oklahoma*, 441 U.S. 322 (1979), the Court restated this prong of the *Pike* test expressly in terms of discrimination: “whether alternative means could promote this local purpose as well without discriminating against interstate commerce.” *Id.* at 336.

¹¹⁷ *Dean Milk Co. v. City of Madison*, 340 U.S. 349, 354 (1951).

least-intrusive-means test applies a rigid bottom line to an otherwise flexible standard.

In *Hughes v. Oklahoma*,¹¹⁸ an Oklahoma statute prohibiting the interstate sale of Oklahoma minnows was challenged on commerce clause grounds.¹¹⁹ After finding that the law facially discriminated against interstate commerce,¹²⁰ the Court unequivocally stated: "At a minimum such facial discrimination invokes the strictest scrutiny of any purported legitimate local purpose and of the absence of nondiscriminatory alternatives."¹²¹ The Court's language strongly implies that the least-intrusive-means requirement of *Pike* is, like the strict scrutiny standard found in the equal protection cases, virtually impossible to overcome.¹²² The difficulty for the state is compounded by the fact that *Hughes*'s "strictest scrutiny" goes not just to the offending regulation, but to the entire spectrum of possibly less intrusive regulations.

The essential lesson from the regulation cases is twofold. First, to

¹¹⁸ 441 U.S. 322 (1979).

¹¹⁹ *Hughes* expressly overruled *Geer v. Connecticut*, 161 U.S. 519 (1896), which had held that because the state "owned" the wild game within its borders, the state's control over the game was outside the scope of the commerce clause. 441 U.S. at 335; see *Geer v. Connecticut*, 161 U.S. at 530-32. By overruling *Geer*, *Hughes* removed the only barrier to commerce clause scrutiny of the Oklahoma statute.

¹²⁰ "It forbids the transportation of natural minnows out of the State for purposes of sale, and thus 'overtly blocks the flow of interstate commerce at [the] State's borders.'" 441 U.S. at 336-37 (quoting *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978)).

¹²¹ *Id.* at 337. Applying this strict scrutiny, the Court held the statute repugnant to the commerce clause because "Oklahoma ha[d] chosen to 'conserve' its minnows in the way that most overtly discriminate[d] against interstate commerce." *Id.* at 338.

¹²² The strict scrutiny standard of the equal protection cases has been criticized as a result-oriented label that virtually seals the fate of the challenged regulation. Gunther, *The Supreme Court, 1971 Term—Foreword: In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1, 8 (1972). "[T]here are very few cases which strictly scrutinize and yet uphold instances of impaired fundamental rights." L. TRIBE, *supra* note 17, § 16-6, at 1000.

As recently put by Justice Blackmun:

I have never been able fully to appreciate just what a "compelling state interest" is. If it means "convincingly controlling," or "incapable of being overcome" upon any balancing process, then, of course, the test merely announces an inevitable result, and the test is no test at all. And, for me, "least drastic means" is a slippery slope and also the signal of the result the Court has chosen to reach. A judge would be unimaginative indeed if he could not come up with something a little less "drastic" or a little less "restrictive" in almost any situation, and thereby enable himself to vote to strike legislation down.

Illinois State Bd. of Elections v. Socialist Workers Party, 440 U.S. 173, 188-89 (1979) (Blackmun, J., concurring).

survive a commerce clause challenge, a state regulation must either be nondiscriminatory or be the least discriminatory means of achieving an important state objective. Second, even if nondiscriminatory, the regulation must be judged by balancing the importance of the state interest it serves against the burden it imposes on interstate commerce. The Court's efforts in the state regulation cases to accommodate both state and federal interests through a balancing test are a far cry from the mechanical severance-precedes-commerce test applied in *Heisler*. As will be seen below, the resource isolation cases further erode the *Heisler* trilogy.

B. *The Resource Isolation Cases*

The Supreme Court has characterized certain state regulations as placing the state "in a position of economic isolation"¹²³ that effectuates economic protectionism¹²⁴ or tends towards "economic Balkanization."¹²⁵ Such a characterization leads to the inescapable conclusion that the particular regulation erects precisely the kind of barrier that the commerce clause was designed to prohibit.¹²⁶ The Court consistently has used this analysis in cases that involve the isolation of a state's natural resources from interstate business and consumers in sister states.¹²⁷

In an early resource isolation case, *West v. Kansas Natural Gas Co.*,¹²⁸ the Court was confronted with an Oklahoma statute that in effect prohibited the shipment of natural gas outside the state. The Court struck down the statute as purposeful discrimination against interstate commerce.¹²⁹ In doing so, it rejected the argument that the

¹²³ *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

¹²⁴ *H.P. Hood & Sons v. Du Mond*, 336 U.S. 525 (1949).

¹²⁵ *Hughes v. Oklahoma*, 441 U.S. 322, 325 (1979); see Friedman, Hardy & Wuliger, *Balkanization of Interstate Energy Markets: New Variations of Sovereign Self-Interest*, 30 CASE W. RES. L. REV. 291 (1980).

¹²⁶ *E.g.*, *Hughes v. Oklahoma*, 441 U.S. 322 (1979); *Philadelphia v. New Jersey*, 437 U.S. 617 (1978); see text accompanying notes 18-30 *supra*.

¹²⁷ Similarly, the Court has invalidated an attempt by Mississippi to withhold its markets from producers in a sister state that did not provide reciprocal rights to Mississippi producers. *Great Atl. & Pac. Tea Co. v. Cottrell*, 424 U.S. 366 (1976). The Mississippi regulation was invalid because it invited "a multiplication of preferential trade areas destructive of the very purpose of the Commerce Clause." *Id.* at 380 (quoting *Dean Milk Co. v. City of Madison*, 340 U.S. 349, 356 (1951)). Relying on the free trade concept that underlies the commerce clause, *id.* at 380; see text accompanying notes 18-25 *supra*, the Court reasoned that the commerce clause precludes "the threat of economic isolation as a weapon to force sister states to enter into even a desirable reciprocity agreement." 424 U.S. at 379.

¹²⁸ 221 U.S. 229 (1911).

¹²⁹ *Id.* at 262. The Court relied on the logic of *State ex rel. Corwin v. Indiana & Ohio Oil, Gas & Mining Co.*, 120 Ind. 575, 22 N.E. 778 (1889), an Indiana case that had invalidated a similar law. The *Corwin* court had reasoned as follows:

state had the right to reserve its resources for the use of its citizens.¹³⁰ Similarly, when West Virginia sought to prevent natural gas pipeline companies from shipping natural gas out of the state until all local needs were met, the Court in *Pennsylvania v. West Virginia*¹³¹ held that the commerce clause prohibited the state's "attempt to regulate the interstate business to the advantage of the local consumers."¹³² The Court in these early cases did not reject conservation of natural resources as a legitimate state end,¹³³ but it did preclude the use of trade barriers as legitimate means to that end.

These resource isolation cases can be analyzed under the least-intrusive-means component of the *Pike* test.¹³⁴ First, they present classic examples of state regulations that discriminate against interstate commerce.¹³⁵ Second, although these regulations may serve legitimate local purposes,¹³⁶ they do so without regard to less discriminatory alternatives.¹³⁷ Indeed, they impose the ultimate burden on interstate commerce by preventing certain resources from ever entering interstate commerce. For this reason, the balancing component of the *Pike* test

(1) when brought to the surface and put in pipes, natural gas is a "commercial product" that can be transported, bought, and sold; (2) if natural gas can be kept in a state, so can all other commercial products such as corn, wheat, lead, and iron, which would result in the "annihilation of interstate commerce"; and (3) therefore, the statute prohibiting shipment out of state violates the commerce clause. 221 U.S. at 256 (quoting *Corwin*, 120 Ind. at 578, 22 N.E. at 779).

¹³⁰ *Id.* at 250.

¹³¹ 262 U.S. 553 (1923).

¹³² *Id.* at 597-98. "A State is without power to prevent privately owned articles of trade from being shipped and sold in interstate commerce on the ground that they are required to satisfy local demands or because they are needed by the people of the State." *Foster-Fountain Packing Co. v. Haydel*, 278 U.S. 1, 10 (1928). In addition to regulations that favor local customers, those whose purpose or effect is to favor local producers have been invalidated on commerce clause grounds. *E.g.*, *Hunt v. Washington State Apple Advertising Comm'n*, 432 U.S. 333 (1977); *H.P. Hood & Sons v. Du Mond*, 336 U.S. 525 (1948); *Toomer v. Witsell*, 334 U.S. 385 (1948).

¹³³ The modern cases, of course, specifically recognize "the States' interests in conservation . . . as legitimate local purposes similar to the States' interests in protecting the health and safety of their citizens." *Hughes v. Oklahoma*, 441 U.S. 322, 337 (1979). Nondiscriminatory regulations aimed at conservation will therefore survive commerce clause scrutiny. In *Cities Serv. Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179 (1950), the Supreme Court let stand a state-imposed increase in oil wellhead prices as a valid measure to discourage the wasting of gas. The Court concluded that "[i]nsofar as conservation is concerned, the national interest and the interest of producing states may well tend to coincide." *Id.* at 187-88.

¹³⁴ See text accompanying notes 115-22 *supra*.

¹³⁵ See text accompanying notes 79-86 *supra*.

¹³⁶ See text accompanying notes 87-103 *supra*.

¹³⁷ See text accompanying notes 115-22 *supra*.

does not apply; once the Court finds the evil of resource isolationism, the statute almost inevitably falls.

This analysis appears most clearly in *City of Philadelphia v. New Jersey*.¹³⁸ There, the Court invalidated a New Jersey law that sought to protect the state's diminishing sanitary land fills by banning the importation of garbage. Rather than focusing on the article of commerce (the garbage), the Court looked to the scarce natural resource (New Jersey's land fill).¹³⁹ After characterizing the landfill as a resource, the Court easily found the "evil of protectionism"¹⁴⁰ in the statute that precluded interstate access to the resource.¹⁴¹ The Court then applied "a virtually *per se* rule of invalidity."¹⁴² More recently, in *Hughes v. Oklahoma*,¹⁴³ the Court again demonstrated that if trade barrierism or resource isolationism is found, the *Pike* balancing test does not apply. *Hughes* makes clear that the Court will apply "the strictest scrutiny" when it finds resource isolationism.¹⁴⁴

¹³⁸ 437 U.S. 617 (1978).

¹³⁹ *Id.* at 628.

¹⁴⁰ *Id.* at 626.

It is interesting to note that in *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980), the Court sidestepped the resource isolationism argument. "Cement is not a natural resource, like coal, timber, wild game, or minerals. It is the end product of a complex process whereby a costly physical plant and human labor act on raw materials." *Id.* at 443-44 (citations omitted). This distinction was challenged by Justice Powell in dissent.

The Court's distinction fails in two respects. First, the principles articulated in the natural resources cases also have been applied in decisions involving agricultural production, notably milk processing. More fundamentally, the Court's definition of cement production describes all sophisticated economic activity, including the exploitation of natural resources. The extraction of natural gas, for example, could hardly occur except through a "complex process whereby a costly physical plant and human labor act on raw materials."

Id. at 449 n.2 (Powell, J., dissenting) (citations omitted). The result in *Reeves* suggests that the evil of resource isolationism can best be avoided by labeling the product at issue as something other than a "resource."

¹⁴¹ Consequently, the Court found it unnecessary to reach the *Pike* balancing test. "This dispute about ultimate legislative purpose need not be resolved, because its resolution would not be relevant to the constitutional issue to be decided in this case." 437 U.S. at 626.

¹⁴² *Id.* at 624, 628.

¹⁴³ 441 U.S. 322 (1979).

¹⁴⁴ *Id.* at 337; see text accompanying notes 118-22 *supra*. The evil of resource isolationism is that it discriminates against interstate commerce by preventing certain resources from entering commerce. See text accompanying notes 134-37 *supra*. Justice Rehnquist takes the view, however, that such discrimination does not violate the commerce clause unless it favors in-state business over out-of-state business, "no matter how 'Balkanized' the resulting pattern of commercial activity." *Hughes v. Oklahoma*, 441 U.S. at 342-43 (Rehnquist, J., dissenting). He thus rejects the strict scrutiny standard in resource isolation cases and would

The resource isolation cases undercut the application of the *Heisler* trilogy to modern resource taxation problems. State taxation may be viewed as a form of state regulation that can isolate state resources.¹⁴⁵ If a severance tax is so high that it actually precludes or hinders access to the needed resource, the specter of resource isolationism and its attendant discrimination clearly is raised.¹⁴⁶ Consequently, the tax may trigger the strict scrutiny test of *Hughes* or the per se rule of *City of Philadelphia*.¹⁴⁷ As modern severance tax rates continue to rise, the *Heisler* trilogy becomes less likely to shield them from charges of resource isolationism.

C. The State Taxation of Commerce Cases

The decisions governing state taxation of commerce are the quiet revolution in current constitutional adjudication. Recent Supreme Court rulings in *Department of Revenue v. Association of Washington Stevedoring Cos.*,¹⁴⁸ *Complete Auto Transit, Inc. v. Brady*,¹⁴⁹ and *Michelin Tire Corp. v. Wages*¹⁵⁰ have rewritten the ground rules in this field. A brief review of the previous law is necessary to understand these decisions.¹⁵¹

One early touchstone of commerce clause adjudication was the principle that the privilege of doing interstate business could not be subject to state taxation. The Court began with the notion that the commerce clause prevented a state from entirely barring an out-of-state corporation from doing interstate business within the state.¹⁵² It then extended

simply apply the *Pike* balancing test to weigh the governmental interest involved against the degree of the burden on commerce. *Id.* at 343. *See also* Hellerstein, *Hughes v. Oklahoma: The Court, the Commerce Clause, and State Control of Natural Resources*, 1979 SUP. CT. REV. 51.

¹⁴⁵ “[A] tax might be explained in terms of its regulatory impact, as license taxes sometimes are. Taxes thus justified raise the same issues as do state regulations and are therefore judged by the [same] standards.” L. TRIBE, *supra* note 17, § 6-14, at 346.

¹⁴⁶ State taxes “used . . . with the aim and effect of establishing an economic barrier” clearly suffer from the same constitutional infirmity as trade barrier regulations. *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

¹⁴⁷ Given the result-oriented nature of a strict scrutiny standard, *see* note 122 *supra*, the difference between the strict scrutiny approach articulated in *Hughes* and the per se approach of *City of Philadelphia* may have little or no practical significance. Perhaps it is not unlike the difference between an irrebuttable presumption (*City of Philadelphia*) and a presumption rebuttable in law but in fact insurmountable (*Hughes*).

¹⁴⁸ 435 U.S. 734 (1978).

¹⁴⁹ 430 U.S. 274 (1977).

¹⁵⁰ 423 U.S. 276 (1976).

¹⁵¹ The brief review that follows is a distillation of the review found in Hellerstein, *State Taxation and the Supreme Court: Toward a More Unified Approach to Constitutional Adjudication*, 75 MICH. L. REV. 1426, 1442-45 (1977).

¹⁵² *Pensacola Tel. Co. v. Western Union Tel. Co.*, 96 U.S. 1 (1877).

the principle to bar a tax imposed on a foreign corporation as a condition to doing business within a state.¹⁵³ From there it took only a small step to prohibit taxes levied on the privilege of conducting interstate business.¹⁵⁴

Early in the development of the privilege doctrine, the Court began to sidestep the doctrine by labeling certain aspects of business (such as the manufacture of goods,¹⁵⁵ the mining or severance of mineral resources,¹⁵⁶ and the generation of power¹⁵⁷) as "local incidents" of interstate business. These "local incidents" were taxable because they "preceded" interstate commerce and therefore were not subject to commerce clause limitations. In applying the privilege doctrine, the Court commonly looked to whether a particular tax was levied on local incidents of interstate business or on the privilege of conducting interstate business.

The Court soon became caught in an illusory search for a principled way to make this distinction. In *Spector Motor Service, Inc. v. O'Connor*,¹⁵⁸ it struck down a corporate tax on net income received within the state. As applied to a foreign corporation engaged exclusively in interstate commerce, the tax amounted to a tax on the privilege of doing interstate business and thus violated the commerce clause.¹⁵⁹ In *Northwestern States Portland Cement Co. v. Minnesota*,¹⁶⁰ however, the Court upheld taxes identical in their economic effects to the tax at issue in *Spector Motor*, stating that these taxes were not privilege taxes.¹⁶¹ This formalistic application of the privilege doctrine virtually determined the validity of a particular tax according to the name the state legislature gave it.¹⁶²

¹⁵³ See *Western Union Tel. Co. v. Kansas ex rel. Coleman*, 216 U.S. 1 (1910).

¹⁵⁴ See, e.g., *Memphis Steam Laundry Cleaner, Inc. v. Stone*, 342 U.S. 389 (1952); *Alpha Portland Cement Co. v. Massachusetts*, 268 U.S. 203 (1925).

¹⁵⁵ E.g., *American Mfg. Co. v. St. Louis*, 250 U.S. 459 (1919); *United States v. E. C. Knight Co.*, 156 U.S. 1 (1895).

¹⁵⁶ E.g., *Heisler v. Thomas Colliery Co.*, 260 U.S. 245 (1922); see text accompanying notes 55-62 *supra*.

¹⁵⁷ *Utah Power & Light Co. v. Pfost*, 286 U.S. 165 (1932).

¹⁵⁸ 340 U.S. 602 (1951).

¹⁵⁹ *Id.* at 609.

¹⁶⁰ 358 U.S. 450 (1959).

¹⁶¹ *Id.* at 462.

¹⁶² Compare *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954) (tax on "privilege of doing business" held invalid), with *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434 (1959) (upholding the same tax relabeled as a "franchise tax"). The formalistic focus on the legislative labeling of a tax rather than its economic effect reached its highwater mark in *Colonial Pipeline, Inc. v. Traigle*, 421 U.S. 100 (1975). The Court in *Colonial Pipeline* upheld a tax on the privilege of doing interstate business *in corporate form*, while at the same time it reaffirmed the *Spector Motor* holding that a tax on the privilege of doing interstate business itself violated the commerce clause. Indeed, *Colonial Pipeline*

The break from the privilege doctrine came in *Complete Auto Transit, Inc. v. Brady*.¹⁶³ *Complete Auto* overruled the *Spector Motor* test and stated that the Court had “moved toward a standard of permissibility of state taxation based upon its actual effect rather than its legal terminology.”¹⁶⁴ In upholding a Mississippi tax on the “privilege of doing interstate business,” the Court enunciated a four-pronged, functional test: a state tax does not violate the commerce clause when it “[1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State.”¹⁶⁵

had successfully challenged an earlier state tax on the privilege of doing business. *Colonial Pipeline Co. v. Morton*, 228 So. 2d 718 (La. Ct. App. 1969), *review denied*, 255 La. 474, 231 So. 2d 393 (1970). The Louisiana legislature then changed the words “the privilege of carrying on or doing business” to “[t]he qualification to carry on or do business in this state or the actual doing of business within this state in a corporate form.” 421 U.S. at 103 (quoting Act of July 13, 1970, ch. 325, § 1, 1970 La. Acts 856 (amending LA. REV. STAT. ANN. § 47:601 (1970))). When this second form of the statute was challenged, it was upheld. 421 U.S. at 109-14.

¹⁶³ 430 U.S. 274 (1977).

¹⁶⁴ *Id.* at 281.

¹⁶⁵ *Id.* at 279. The replacement of the formalistic approach with the practical-effect doctrine of *Complete Auto* was foreshadowed by the Court’s decision in *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976). In *Michelin Tire*, the Court disavowed the century-old, mechanistic “original package” doctrine, *see note 37 supra*, and held that the import-export clause did not bar a state from imposing a nondiscriminatory ad valorem property tax on imported goods. 423 U.S. at 282-83. In doing so, the Court applied the following practical analysis:

To be sure, allowance of nondiscriminatory ad valorem property taxation may increase the cost of goods purchased by “inland” consumers. But as already noted, such taxation is the *quid pro quo* for benefits actually conferred by the taxing State. There is no reason why local taxpayers should subsidize the services used by the importer; ultimate consumers should pay for such services as police and fire protection accorded the goods just as much as they should pay transportation costs associated with those goods. An evil to be prevented by the Import-Export Clause was the levying of taxes which could only be imposed because of the peculiar geographical situation of certain States that enabled them to single out goods destined for other States. In effect, the Clause was fashioned to prevent the imposition of exactions which were no more than transit fees on the privilege of moving through a State. A nondiscriminatory ad valorem property tax obviously stands on a different footing, and to the extent there is any conflict whatsoever with this purpose of the Clause, it may be secured merely by prohibiting the assessment of even nondiscriminatory property taxes on goods which are merely in transit through the State when the tax is assessed.

Id. at 288-90 (footnotes omitted). The Court in *Department of Revenue v. Association of Wash. Stevedoring Cos.*, 435 U.S. 734, 755 (1978), held that a nondiscriminatory tax on gross receipts from the stevedoring of goods in transit would not be invalid under the import-export clause.

The *Complete Auto* test was reaffirmed the following year in *Department of Revenue v. Association of Washington Stevedoring Cos.*¹⁶⁶ Reversing earlier stevedoring cases,¹⁶⁷ *Washington Stevedoring* held that "taxing the interstate commerce activity of stevedoring" does not necessarily violate the commerce clause.¹⁶⁸ Rather, "[t]he Commerce Clause balance tips against the tax only when it unfairly burdens commerce by exacting more than a just share from the interstate activity."¹⁶⁹ It is, then, the functional test of *Complete Auto* that now governs state taxation of interstate commerce.¹⁷⁰ Each of the test's four elements must be examined in light of earlier Supreme Court cases in order to understand the consequences of applying the test to severance taxation.

1. Substantial Nexus with the State

The requirement of substantial nexus, or "minimum contacts," between the state and the activity taxed is as much a due process limitation on jurisdiction as it is a requirement of the commerce clause.¹⁷¹ In addition to the notions of fairness embodied in the due process clause,¹⁷² the nexus requirement demanded by current commerce clause doctrine serves two important purposes.¹⁷³ First, it ensures that the tax will have some impact on local as well as interstate interests. Local impact guarantees that the political restraints of a state's legislative process will come into play.¹⁷⁴ Second, the nexus requirement reduces the risk that the tax will place an undue cumulative burden on interstate commerce.¹⁷⁵ The more directly the tax is connected with local activities

¹⁶⁶ 435 U.S. 734 (1978).

¹⁶⁷ *Joseph v. Carter & Weekes Stevedoring Co.*, 330 U.S. 422 (1947); *Puget Sound Stevedoring Co. v. State Tax Comm'n*, 302 U.S. 90 (1937).

¹⁶⁸ 435 U.S. at 749-50. The Court also applied *Michelin Tire* to uphold the tax against an import-export clause attack. *Id.* at 759-61.

¹⁶⁹ *Id.* at 748. When it applied the four elements of the *Complete Auto* test, the Court found "no factual basis on which to declare the Washington tax unconstitutional." *Id.* at 751.

¹⁷⁰ See *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979).

¹⁷¹ Compare *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967) (use tax invalidly applied because minimum contacts requirement of commerce clause not met), with *American Oil Co. v. Neil*, 380 U.S. 451 (1965) (sales tax invalid because the state lacked minimum contacts required by due process).

¹⁷² See, e.g., *International Shoe v. Washington*, 326 U.S. 310 (1945).

¹⁷³ See *L. TRIBE*, *supra* note 17, §§ 6-14 to -15.

¹⁷⁴ "Lying back of these decisions is the recognized danger that, to the extent that the burden falls on economic interests without the state, it is not likely to be alleviated by those political restraints which are normally exerted on legislation where it affects adversely interests within the state." *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 45 n.2 (1940).

¹⁷⁵ The main evil of cumulative burdens on commerce is that they discriminate against interstate commerce and thus erect barriers to interstate trade. See *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 256 (1938). Generally, the

and events, the less likely it is that other states will impose the same tax;¹⁷⁶ consequently, there is less risk of cumulative tax burdens.¹⁷⁷

2. Fair Apportionment

The fair apportionment requirement is aimed primarily at preventing the cumulative taxation of interstate commerce. To meet this requirement, the taxing state must set its tax on an interstate business according to a formula that fairly determines the fraction of the total business that takes place within the taxing state. As formulated by the Court, the fair apportionment requirement asks whether “what the State is exacting is a constitutionally fair demand by the State for that aspect of the interstate commerce to which the State bears a special relation.”¹⁷⁸ Thus, the fair apportionment doctrine addresses some of the same considerations of fairness, free trade, and multiple burden as the nexus requirement.¹⁷⁹ One significant difference, however, is that this element

taxpayer must prove that a cumulative burden actually exists. *General Motors Corp. v. Washington*, 377 U.S. 436 (1964). At least one Supreme Court decision has indicated, however, that proof of a clear *potential* for an extreme cumulative burden is sufficient to invalidate a state tax. *See National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753, 759 (1967) (“For if Illinois can impose such burdens, so can any other State, and so, indeed, can . . . every other political subdivision throughout the Nation with power to impose sales and use taxes.”).

¹⁷⁶ *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 260 (1938). Interestingly, one offshoot of the reasoning of the *Heisler* trilogy is the notion that because the act of severance precedes movement in interstate commerce, resource severance taxes do not lend themselves to multiple application.

¹⁷⁷ The strong local nexus of certain fixed-fee taxes has been sufficient to justify them as providing reasonable compensation for benefits conferred, despite their capability of multiple application. *E.g.*, *Evansville-Vanderburgh Airport Auth. Dist. v. Delta Airlines, Inc.*, 405 U.S. 707 (1972) (tax of \$1.00 per passenger levied on airlines using state airports was sufficiently related to benefit).

¹⁷⁸ *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653, 661 (1948). The formula “must bear a rational relationship, both on its face and in its application, to . . . values connected with the taxing State.” *Norfolk & W. Ry. v. Missouri State Tax Comm’n*, 390 U.S. 317, 325 (1968) (formula’s reliance on track mileage led to demonstrably inflated tax).

Although the fair apportionment principle in theory prevents the repeated taxation of the same local incident, the use of diverse formulae by different states leads to overlapping tax liabilities. *See* L. TRIBE, *supra* note 17, § 6-19. The Court’s efforts to avoid such cumulative burdens have resulted in the requirement that an apportionment formula include more than one measure of business activity. The net income tax upheld in *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 453-54 (1959), involved three measures of business activity: sales, total tangible property, and payroll. *But see Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978).

The Court has also suggested that unusual formulae may be subject to closer scrutiny to ensure that multiple burdens are avoided. *General Motors Corp. v. District of Columbia*, 380 U.S. 553, 559-60 (1965); *see* L. TRIBE, *supra* note 17, § 6-19.

¹⁷⁹ Professor Tribe properly points out that fair apportionment does not allevi-

of the *Complete Auto* test addresses the amount of the tax as distinguished from the power or right of the state to impose the tax.

3. *Nondiscrimination*

In order to prevent balkanization of the states, the commerce clause has been used consistently to strike down state taxes that unreasonably benefit local commerce at the expense of interstate commerce. Taxes that unjustifiably encourage the conduct of business operations within the taxing state¹⁸⁰ and those that exempt in-state activities or persons without sufficient justification¹⁸¹ are but two examples of the kinds of discrimination against interstate commerce that the commerce clause prohibits. Furthermore, as in the state regulation cases,¹⁸² the discrimination need not be facial. The Court will probe to uncover discriminatory effects of seemingly neutral statutes.¹⁸³

Competitive disadvantage to out-of-state businesses is the principal concern of the nondiscrimination aspect of the *Complete Auto* test.¹⁸⁴ The inability of out-of-state merchants and consumers to participate in local tax decisions, however, provides another reason for commerce clause protection from discriminatory barriers designed to protect local business.¹⁸⁵ Nevertheless, the mere fact that the impact of the tax may be passed on to out-of-state users of the ultimate product does not constitute discrimination.¹⁸⁶

ate the "tollgatism" created by taxes that merely capitalize on a strategic trade route. L. TRIBE, *supra* note 17, § 6-18, at 365 n.16.

¹⁸⁰ *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318 (1977). The tax under attack, which encouraged the selling of stocks in New York, was markedly similar to the law in *Pike*, which encouraged the boxing of cantaloupes in Arizona. *Id.* at 335-36.

¹⁸¹ *Hale v. Bimco Trading, Inc.*, 306 U.S. 375 (1939). The electrical energy tax in *Arizona Pub. Serv. Co. v. Snead*, 441 U.S. 141 (1979), was similarly invalidated because of an unjustifiable local exemption, although the case was ultimately decided on federal preemption grounds.

¹⁸² See text accompanying note 86 *supra*.

¹⁸³ See, e.g., *Best & Co. v. Maxwell*, 311 U.S. 454 (1940). *Alaska v. Arctic Maid*, 366 U.S. 199 (1961), suggests that in the case of a facially discriminatory statute, the Court will look for a nondiscriminatory effect. *But see Arizona Pub. Serv. Co. v. Snead*, 441 U.S. 141 (1979).

¹⁸⁴ *Robbins v. Shelby County Taxing Dist.*, 120 U.S. 489, 498 (1887) (solicitation fee operated to disadvantage of out-of-state businesses).

¹⁸⁵ The Court in *Nippert v. City of Richmond*, 327 U.S. 416 (1946), struck down a local solicitation license tax because of its discriminatory and exclusionary effects. "Provincial interests and local political power are at their maximum weight in bringing about acceptance of this type of legislation. With the forces behind it, this is the very kind of barrier the commerce clause was put in the fundamental law to guard against." *Id.* at 434.

¹⁸⁶ See, e.g., *Heisler v. Thomas Colliery Co.*, 260 U.S. 245 (1922); *Coe v. Errol*, 116 U.S. 517 (1886).

4. Fair Relationship to Services

The *Complete Auto* requirement that the tax be “fairly related to the services provided by the State”¹⁸⁷ has its origins in earlier nexus cases.¹⁸⁸ The Court has framed the issue as “whether the State has exerted its power in proper proportion to [the taxpayer’s] activities within the State and to [the taxpayer’s] *consequent enjoyment of the opportunities and protections* which the State has afforded”¹⁸⁹ or, more simply, “whether the state has given anything for which it can ask return.”¹⁹⁰

These formulations of the fair-relationship-to-services requirement were couched in terms of “nexus” to the taxing state; commentators have similarly connected the two requirements.¹⁹¹ However, *Complete Auto*’s articulation of the fair relationship and nexus requirements as separate elements suggests that they are not identical.¹⁹² The Court has recently stated in *Japan Line, Ltd. v. County of Los Angeles*¹⁹³ that the fair-relationship-to-services requirement is indeed an independent element of the *Complete Auto* test, requiring separate proof.¹⁹⁴

Unlike the nexus and discrimination requirements, which merely address the state’s authority to tax, the fair-relationship-to-services requirement limits the amount of the tax. After *Complete Auto* expressly removed the barrier to a direct tax on interstate commerce, some

¹⁸⁷ 430 U.S. at 279.

¹⁸⁸ See text accompanying notes 233–40 *infra*.

¹⁸⁹ *General Motors Corp. v. Washington*, 377 U.S. 436, 441 (1964) (emphasis added). For other Supreme Court formulations of the fair-relationship-to-services requirement, see note 240 and text accompanying notes 233–43 *infra*.

¹⁹⁰ *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 (1940); *cf. Massachusetts v. United States*, 435 U.S. 444, 462–63 (1978):

A governmental body has an obvious interest in making those who specifically benefit from its services pay the cost and, provided that the charge is structured to compensate the government for the benefit conferred, there can be no danger of the kind of interference with constitutionally valued activity that the Clauses were designed to prohibit.

Id. at 462–63.

¹⁹¹ To assess the significance of a state’s compensatory interest in the application of its tax to a particular taxpayer, one must determine the degree to which the taxpayer’s activities in interstate commerce benefit from state government services. And, as a rough but constitutionally adequate measure of benefits conferred, one must look to the ways in which the taxed activities can be “connected” with the taxing state.

L. TRIBE, *supra* note 17, § 6–14, at 346.

¹⁹² *Complete Auto* was followed by a similar formulation of the fair-relationship-to-services requirement as a separate element requiring distinct proof in *Department of Revenue v. Association of Wash. Stevedoring Cos.*, 435 U.S. 734, 750 (1978).

¹⁹³ 441 U.S. 434 (1979).

¹⁹⁴ *Id.* at 445.

mechanism was needed to control taxes that were so excessive as to be confiscatory and barrier-creating, yet had sufficient connection to the taxing state, were nondiscriminatory, and were not subject to apportionment. That mechanism was the fair-relationship-to-services requirement, adapted from the nexus rationale of the earlier cases and elevated to an independent element of the current commerce clause test. When the Court ultimately faces the commerce clause questions raised by modern resource taxation, it is this requirement that will serve as the constitutional measuring rod.

IV

Heisler RECONSIDERED IN THE MODERN CONTEXT

The rigid formalism that characterized early commerce clause cases first gave way to a balancing of state and federal interests in the state regulation cases. This section of the Article will demonstrate that the Court has adopted that same balancing approach in the state taxation cases and that this development seriously erodes the formalistic underpinnings of the *Heisler* severance-precedes-commerce analysis. Thus, *Heisler* will be of dubious support when state resource severance taxes come before the modern Court.

Originally, state taxation was shielded from a balancing approach by the twin notions that (1) states could not tax the conduct of interstate business,¹⁹⁵ and (2) state taxes had to attach to "local incidents" of business activities.¹⁹⁶ In *Complete Auto*, the Court overturned the first of these principles.¹⁹⁷ Applying "a standard of permissibility of state taxation based on its actual effect rather than its legal terminology," the Court balanced the state's tax against the services the state provided.¹⁹⁸

Only a year later, in *Washington Stevedoring*,¹⁹⁹ the Court clearly demonstrated that the balancing required by *Pike* in the regulation cases is essentially the same as the balancing that *Complete Auto* demands in the taxation cases. Citing *Southern Pacific Co. v. Arizona*,²⁰⁰ the Court flatly stated that the question of whether a tax burdens commerce is one that requires a balancing of state and federal interests.²⁰¹

¹⁹⁵ See text accompanying notes 152-54 *supra*.

¹⁹⁶ See text accompanying notes 155-57 *supra*. By definition, "local incidents" are those business activities that precede commerce. *Id.*

¹⁹⁷ By implication, *Complete Auto* also overturned the second principle. See text accompanying notes 212-14 *infra*.

¹⁹⁸ 430 U.S. at 281.

¹⁹⁹ 435 U.S. 734 (1978).

²⁰⁰ 325 U.S. 761 (1945).

²⁰¹ 435 U.S. at 748. In *Southern Pacific*, the competing interests were the federal interest in unimpeded train travel and the state interest in safety. See note 109 and text accompanying notes 108-09 *supra*.

Although the balancing of safety interests [at issue in *Southern Pacific*] naturally differs from the balancing of state financial needs, *Complete Auto* recognized that a State has a significant interest in exacting from interstate commerce its fair share of the cost of state government. All tax burdens do not impermissibly impede interstate commerce. The Commerce Clause balance tips against the tax only when it unfairly burdens commerce by exacting more than a just share from the interstate activity.²⁰²

Implicit in this statement is the understanding that the legitimacy-of-the-local-interest and the burden-on-commerce elements of the *Pike* test merge in the *Complete Auto* requirement that a tax be fairly related to services provided by the state.²⁰³ As articulated in *Washington Stevedoring*, the state regulation and state taxation balancing tests both measure the same thing: the essential balance between the burden on commerce and the local governmental interest served.²⁰⁴

The merger of the legal analyses employed in the state regulation and taxation cases has eroded the policy reasons behind the *Heisler* holding. These policy concerns were bound up with the notion that if states were not allowed to tax the production and manufacturing processes within their borders, they would be deprived of essential revenues. As articulated by the Court in *Coe v. Errol*,²⁰⁵ “[i]f such were the rule in many States there would be nothing but the lands and real estate to bear the taxes.”²⁰⁶ In addition, the *Heisler* Court felt that a refusal to allow state taxation of production and manufacturing would be contrary to principles of federalism because it would withdraw from the states

²⁰² 435 U.S. at 748 (citations omitted).

²⁰³ Similarly, the evenhandedness element of *Pike* is identical to the nondiscrimination prong of the *Complete Auto* test. Although the least-intrusive-means principle of *Pike* does not match any stated element of *Complete Auto*, it speaks to the same trade barrierism issues as the discrimination element of *Complete Auto*. “Neither the power to tax nor the police power may be used by the state of destination with the aim and effect of establishing an economic barrier against competition with the products of another state or the labor of its residents.” *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

²⁰⁴ This merger of the two balancing tests is similarly described in the dissenting opinion of Justice Powell in *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978). Taking issue with the Court’s holding that Iowa’s single-factor sales tax formula did not violate the commerce clause, Justice Powell rooted his dissent in the notion developed in the regulation cases that “the Commerce Clause constrains us to view the State’s interest in retaining this particular levy as against the constitutional preference for an open economy.” *Id.* at 289 (Powell, J., dissenting).

²⁰⁵ 116 U.S. 517 (1886).

²⁰⁶ *Id.* at 527–28. The Court’s concern that the states’ tax bases might be eroded was particularly well founded in an era that predated corporate income tax and other business-related taxes. Indeed, this concern may resurface if current efforts at federal budget cutting cause states to lose the revenue-sharing funds on which local governments have become increasingly dependent.

essential control of the commercial activities within their borders.²⁰⁷

The Court enunciated the *Heisler* principle at a time when all or nothing prevailed. A tax on commerce itself was prohibited by the commerce clause interpretation of the day,²⁰⁸ so if the Court was to allow states to tax certain activities, it had to define those activities as "out of" commerce.²⁰⁹ The *Heisler* Court announced its severance-precedes-commerce rule because of its overriding concern that a decision invalidating Pennsylvania's coal severance tax could apply to defeat not only all severance taxes but all kinds of necessary state business taxes.²¹⁰ It also feared that to define mining as "in" commerce would "nationalize and withdraw from state jurisdiction" not just coal but all the native products of each state.²¹¹

Although the post-*Heisler* Court occasionally indicated that the status of being "in" commerce should not prevent the states from exacting some fair measure of taxation,²¹² it was not until *Complete Auto* that the Court firmly held that interstate commerce did indeed have to pay its own way. *Complete Auto* removes the need for the severance-precedes-commerce test of the *Heisler* trilogy because it allows state taxes to stand even when they attach to business activities inextricably linked with interstate commerce.²¹³ Thus, it shows the way to apply the commerce clause to severance taxation while still allowing important state taxes to stand. By upholding only nondiscriminatory, fairly apportioned taxes that have some nexus with the state and are "fairly related to the services provided by the state," the *Complete Auto* test obviates the *Heisler* Court's chief concern. States can tax interstate commerce, but they must do so fairly.

Complete Auto also removes the other policy reason for *Heisler*. Its

²⁰⁷ See note 58 *supra*.

²⁰⁸ *E.g.*, *Alpha Portland Cement Co. v. Massachusetts*, 268 U.S. 203 (1925).

²⁰⁹ See text accompanying notes 155-58 *supra*.

²¹⁰ See notes 58-59 and accompanying text *supra*.

²¹¹ 260 U.S. at 259-60.

²¹² See, *e.g.*, *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 165-66 (1954) ("Frequently it has been said that interstate business must pay its way . . . and the Court has done more than pay lip service to this idea.")

²¹³ Correlative to the *Complete Auto* principle that states may tax interstate commerce is the notion that so long as a tax is reasonably related to the services provided by the taxing state, there can be no objection that the tax may increase the price of the product for persons in other states. See *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976). In upholding the tax in *Michelin Tire* against a challenge under the import-export clause, the Court reasoned:

To be sure, allowance of nondiscriminatory ad valorem property taxation may increase the costs of goods purchased by "inland" consumers. But as already noted, such taxation is the *quid pro quo* for benefits actually conferred by the taxing State. There is no reason why local taxpayers should subsidize the services used by the importer

Id. at 288-89.

four-pronged test can be read to protect local control and taxation of “the fruits of California and the South, the wheat of the West and its meats, the cotton of the South, the shoes of Massachusetts and the woolen industries of other States”²¹⁴ just as surely as *Heisler* but without the rigid formalism that requires the Court to say that while certain activities are closely linked with commerce, they are not “in” commerce.

Finally, one seemingly small point has crept almost unnoticed into the latest resource isolation cases, which may remove the last remaining analytical defense of the *Heisler* trilogy. While *Complete Auto* has removed the need to define resource severance as “out of” commerce, the resource isolation cases may have broadened the definition of “commerce” itself to include resource severance. Recently, the Court has suggested that the definition of “commerce” for purposes of construing the commerce clause’s limitation on state power is the same as its definition for purposes of construing Congress’s affirmative power to act under the clause.²¹⁵

It is firmly established that Congress can act in a plenary fashion under the commerce clause.²¹⁶ Since *NLRB v. Jones & Laughlin Steel Corp.*,²¹⁷ it has also been clear that this plenary power is applicable whenever Congress finds that the regulated activity has a substantial effect on interstate commerce.²¹⁸ It makes no difference to this “substantial economic effect”²¹⁹ test whether the activity is “in” or “out of” the flow of commerce;²²⁰ an activity may have such an effect even if it is wholly within a state²²¹ and even if the activity *standing alone* would have no economic effect.²²² In contrast to this broad interpretation of the commerce clause’s affirmative grant of power, the negative implica-

²¹⁴ *Heisler v. Thomas Colliery Co.*, 260 U.S. at 259.

²¹⁵ See *Hughes v. Oklahoma*, 441 U.S. 322, 326 n.2 (1979); text accompanying notes 224–27 *infra*.

²¹⁶ *E.g.*, *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 196–97 (1824).

²¹⁷ 301 U.S. 1 (1937).

²¹⁸ *Id.* at 41. Such findings need not be formal; a reasonable belief by Congress that the regulated activity has an economic effect on commerce is sufficient to support commerce power legislation. See, *e.g.*, *Heart of Atlanta Motel, Inc. v. United States*, 379 U.S. 241, 258–59 (1964). Congressional power under the commerce clause is discussed in more detail in the text accompanying notes 254–88 *infra*.

²¹⁹ L. TRIBE, *supra* note 17, § 5–4, at 235–36.

²²⁰ *Maryland v. Wirtz*, 392 U.S. 183 (1968) (upholding the application of the Fair Labor Standards Act to all workers who produce goods for interstate commerce). Although *National League of Cities v. Usery*, 426 U.S. 833, 855 (1976), overruled *Wirtz*, it did not disavow the commerce clause analysis of *Wirtz*. See L. TRIBE, *supra* note 17, § 5–4, at 236 n.18.

²²¹ *E.g.*, *United States v. Rock Royal Co-operative, Inc.*, 307 U.S. 533 (1939).

²²² So long as many similar acts taken in the aggregate would have a substantial economic effect, each individual act is subject to federal regulation. *Wickard v. Filburn*, 317 U.S. 111 (1942).

tion of the clause traditionally has been narrowly construed to prevent state taxation only when the tax *directly affects the flow* of commerce.²²³ In *Hughes v. Oklahoma*,²²⁴ however, in an important footnote, the Court read *City of Philadelphia v. New Jersey*²²⁵ to reject this "two-tiered definition of commerce."²²⁶ The *Hughes* Court, without equivocation, stated that "[t]he definition of 'commerce' is the same when relied on to strike down or restrict state legislation as when relied on to support some exertion of federal control or regulation."²²⁷ If this recent dictum survives to become law, the severance-precedes-commerce test of *Heisler* will give way to the substantial-economic-effect test of *Jones & Laughlin*,²²⁸ removing any doubt that state taxation of natural resource severance is now subject to the commerce clause scrutiny of *Complete Auto*. *Heisler's* "in" versus "out of" commerce distinction finally will be extinct.²²⁹

²²³ *Dunbar-Stanley Studios, Inc. v. Alabama*, 393 U.S. 537 (1969).

²²⁴ 441 U.S. 322 (1979).

²²⁵ 437 U.S. 617 (1978).

²²⁶ 441 U.S. at 326 n.2. The two-tiered definition of commerce was clearly articulated in *Wickard v. Filburn*, 317 U.S. 111 (1942).

Whether the subject of the regulation in question was "production," "consumption," or "marketing" is, therefore, not material for purposes of deciding the question of federal power before us. That an activity is of local character . . . might help in determining whether in the absence of Congressional action it would be permissible for the state to exert its power on the subject matter, even though in so doing it to some degree affected interstate commerce. But even if appellee's activity be local and though it may not be regarded as commerce, it may still, whatever its nature, be reached by Congress if it exerts a substantial economic effect on interstate commerce . . .

Id. at 124-25. In *Douglas v. Seacoast Prods., Inc.*, 431 U.S. 265 (1977), Justice Marshall, writing for the Court, stated: "But these statements [that certain activities precede the flow of commerce] were made in upholding the rights of States to tax what was argued to be interstate commerce. Pronouncements made in that context are not used interchangeably as statements of law where the issue is the power of Congress to regulate under the Commerce Clause." *Id.* at 282 n.17.

²²⁷ 441 U.S. at 326 n.2.

²²⁸ The plaintiffs in *Commonwealth Edison Co. v. State*, No. 42657 (Mont. 1st Jud. Dist. July 27, 1979), *aff'd*, 37 Mont. St. Rep. 1192, 615 P.2d 847, *prob. juris. noted*, 101 S. Ct. 607 (1980) (No. 80-581), unsuccessfully argued that the definition of commerce applicable to the negative implication of the commerce power should be the *Jones & Laughlin* test. *Id.* at 17.

²²⁹ This result may be inevitable in part because, as our society becomes more complex, it becomes more difficult to draw reasoned distinctions between which activities are in commerce and which are not. For example, the Court had difficulty distinguishing between the generation and transmission of electricity in *Utah Power & Light Co. v. Pfof*, 286 U.S. 165 (1932). Similarly, in *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954), the Court's reasoning that the tax at issue went beyond production and attached to the transmission of natural gas was less than persuasive.

The decision in *Arizona Public Service Co. v. Snead*²³⁰ illustrates the potential impact of the *Hughes* footnote. In *Utah Power & Light Co. v. Pfost*,²³¹ the Supreme Court had held that the generation of electricity was not in commerce; therefore, a state tax on electricity generation was beyond commerce clause scrutiny. Congress later passed a statute that prohibited states from taxing the generation or transmission of electricity in a manner that discriminated against out-of-state consumers.²³² In *Arizona Public Service*, New Mexico sought to evade the statute, relying on *Utah Power & Light* to argue that its tax on electricity generation was beyond the scope of Congress's power under the commerce clause. The Supreme Court rejected New Mexico's argument and found that Congress had plenary power under the commerce clause to prohibit state taxation of electricity generation. If, as the *Hughes* footnote suggests, the definition of commerce articulated in *Arizona Public Service* applies to state impediments to commerce as well as to the affirmative exercise of the federal commerce power, then *Arizona Public Service* sub silentio overrules the *Utah Power & Light* holding that the generation of electricity precedes commerce. Such a result would complete the erosion of the analytical base on which *Heisler* stands.

V

FAIR RELATIONSHIP TO COST AND BENEFIT: THE NEW BATTLEGROUND

With the demise of the *Heisler* trilogy, the essential inquiry in resource taxation cases will shift from whether the activity taxed precedes commerce to whether the tax is "fairly related to the services provided by the State."²³³ This fair-relationship-to-services element of the *Com-*

²³⁰ 441 U.S. 141 (1979).

²³¹ 286 U.S. 165 (1932).

²³² Tax Reform Act of 1976, Pub. L. No. 94-455, § 2121(a), 90 Stat. 1914 (codified at 15 U.S.C. § 391 (1976)).

²³³ *Complete Auto Transit, Inc. v. Brady*, 430 U.S. at 279. Plaintiffs unsuccessfully raised the argument that *Complete Auto's* fair-relationship-to-services requirement now governs resource severance taxation in *Commonwealth Edison Co. v. State*, 37 Mont. St. Rep. 1192, 1201, 615 P.2d 847, 855, *prob. juris. noted*, 101 S. Ct. 607 (1980) (No. 80-581).

The court in *Merrion v. Jicarilla Apache Tribe*, 617 F.2d 537 (10th Cir.), *cert. granted*, 101 S. Ct. 71 (1980) (No. 80-11), while upholding a tribal severance tax partly because of a *Heisler* finding that the tax attached to a local activity, expressly recognized that a close connection with interstate commerce would trigger the *Complete Auto* test. The court went on to note:

We need not decide whether a severance tax measured by quantity produced within a single jurisdiction falls within the ambit of this new doctrine. . . . [But if the] *Stevedoring* and *Complete Auto Transit* analysis applied, the only question is whether the tax is fairly related to services provided by the reservation.

Id. at 545 n.4.

plete Auto test is not an entirely new development in commerce clause law; its roots are planted firmly in the due process principles of the early nexus cases.²³⁴

The nexus cases require an inquiry into whether there is a sufficient relationship between the industry taxed and the state to justify imposing the tax. When confronted with a due process claim against a state tax, the Court in the nexus cases has scrutinized the benefits and protections that the state affords the industry and the costs that the industry's presence imposes on the state. A finding of benefits to the industry or costs to the state has invariably proved sufficient to defeat the due process claim.

Wisconsin v. J. C. Penney Co.,²³⁵ a hallmark nexus case, formulated the essential question as "whether the state has given *anything* for which it can ask return."²³⁶ Similarly, the Court in *Freeman v. Hewit*²³⁷ described a justifiable state tax on commerce as one "designed to make such commerce bear a *fair share of the cost of the local government* whose protection it enjoys."²³⁸ The test was alternatively stated in *Memphis Natural Gas Co. v. Stone*²³⁹ as allowing taxes that provide "compensation for the protection *and advantages* rendered to commerce by state governments."²⁴⁰

While *Complete Auto* is the first case to elevate the fair-relationship-to-services requirement to independent status, *J. C. Penney* from the nexus context affords insight into the substance of the requirement.

A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to *opportunities* which it has given, to *protection* which it has afforded, to *benefits* which it has conferred by the fact of being an orderly, civilized society.²⁴¹

Most recently, in *Japan Line, Ltd. v. County of Los Angeles*,²⁴² the Court elaborated that the "opportunities," "protections," and "benefits" contemplated by the fair-relationship-to-services requirement "include not only police and fire protection, but the benefits of a trained work

²³⁴ See text accompanying notes 171-73 *supra*.

²³⁵ 311 U.S. 435 (1940).

²³⁶ *Id.* at 444 (emphasis added).

²³⁷ 329 U.S. 249 (1946).

²³⁸ *Id.* at 253 (emphasis added).

²³⁹ 335 U.S. 80 (1948).

²⁴⁰ *Id.* at 85 (emphasis added). The nexus test was quoted with approval in *Colonial Pipeline, Inc. v. Traigle*, 421 U.S. 100 (1975), which stated the question as whether "the State has provided benefits and protections for those activities for which it is justified in asking a fair and reasonable return." *Id.* at 108.

²⁴¹ 311 U.S. at 444 (emphasis added). See also note 190 *supra*.

²⁴² 441 U.S. 434 (1979).

force and the advantages of a civilized society.”²⁴³

The extraction of natural resources imposes on a state three categories of costs that should fall within the ambit of “services provided by the state” articulated in *Complete Auto*.²⁴⁴ First, extractive activities usually impose certain direct costs on governmental units within the state. These direct costs include the monitoring and regulation of airsheds, watersheds, groundwater aquifers, solid waste disposal, and other environmental features commonly disturbed by extractive activity. They may also include the construction of special roads and other public facilities that do not serve the general public and thus require special funding. Although the exact boundary between special public facilities and those serving the general public may be hazy, the problem is one of degree and is therefore properly subject to legislative definition.

Even with extensive regulation and monitoring of the environmental effects of extractive activities, however, there may remain significant damage to public health and well-being. For example, a mine located in an area of high aesthetic quality may cause a significant loss of aesthetic benefits during the lifespan of the mine and even well beyond it. Although such aesthetic damages may not be readily measured, the large amounts of time and resources that environmentally oriented citizens spend in attempts to reduce or eliminate them reveal their significance. Thus, a second aspect of resource taxation is to ensure compensation for those public damages that environmental regulation and monitoring do not eliminate.

Recompense for the first two categories of costs to the state clearly meets the fair-relationship-to-services requirement. Special roads and other state services to the individuals and firms engaged in resource extraction are literally “services provided by the state” within the meaning of *Complete Auto*. Furthermore, in *Arizona Public Service Co. v. Snead*, the Court made it clear that states may collect taxes to pay for the costs associated with “environmental and other problems” caused by the generation of electricity.²⁴⁵ Therefore, the fair-relationship-to-services requirement of *Complete Auto* must contemplate compensation for the environmental regulation and monitoring and environmental damage associated with the presence of the industry.

The third basis for recompense to the state is the resource extraction itself, rather than its environmental and other side effects. Each of the resources on which the taxes are levied is finite and nonrenewable. As

²⁴³ *Id.* at 445.

²⁴⁴ See generally Note, *supra* note 5.

²⁴⁵ “The generation of electricity in the Four Corners region undoubtedly also generates environmental and other problems for New Mexico. *There is no indication that Congress intended to prevent the state from taxing the generation of electricity to pay for solutions to these problems.*” 441 U.S. 141, 150–51 (emphasis added).

a consequence, the state faces the inevitable depletion of these assets and a subsequent contraction in the state's economy if a sustainable economic base cannot be developed to replace the depleted wealth.²⁴⁶ Even more concretely, state government and other governmental units within the state face the inevitable prospect of a decline in the revenues available to support public services as the taxable resource disappears.²⁴⁷

This third category of costs to the state may fall within the "opportunities" and "benefits" contemplated by *J. C. Penney*²⁴⁸ and *Japan Line*,²⁴⁹ however, quantification becomes a major difficulty.²⁵⁰ Under the modern balancing test mandated by *Complete Auto*, the amount of, as well as the reason for, the tax must be fairly related to the services provided. Thus, courts must determine whether the amount of costs the state claims to have incurred is reasonable. The reasonableness of resource replacement costs is more difficult to determine than that of the direct costs of state services referred to in *Japan Line* and the envi-

²⁴⁶ " 'You can't expect a state to take the environmental risks, lose a nonrenewable resource and not cover its costs,' says Kent Conrad, an aide to Mr. Dorgan [North Dakota tax commissioner]. 'If we can't break even, we'll stop development.' " *Wall St. J.*, Mar. 26, 1980, at 14, col. 2.

²⁴⁷ "Do they really want Montana to become another Appalachia?" asks Wally McRae, a cattle rancher who lives near the town of Colstrip (pop. 1,900). "People are attacking us for doing something we think is responsible. We're sliding along now on a great bubble, but it will burst somewhere down the road. Coal-based economies always go to hell. We're trying to avoid the boom-bust cycle."

Id. col. 1.

²⁴⁸ 311 U.S. at 444; *see* text accompanying note 241 *supra*.

²⁴⁹ 441 U.S. at 445; *see* text accompanying note 243 *supra*.

²⁵⁰ On the other hand, precise mathematical measurement is not required in weighing the amount of tax against the services provided. In a concurring opinion in *Washington Stevedoring*, Justice Powell stated:

[T]he Court observes that "nothing in the record suggests that the tax is not fairly related to services and protection provided by the State." Since the stevedoring companies undoubtedly avail themselves of police and fire protection, as well as other benefits Washington offers its local businesses, this statement cannot be questioned.

435 U.S. at 764 (citation omitted). A similar view was expressed by Justice Blackmun in his concurring opinion in *Raymond Motor Transp., Inc. v. Rice*, 434 U.S. 429, 447 (1978).

Similarly, in the tax apportionment cases, the Court has been reluctant to second-guess state legislative judgments setting the amounts of tax levies. The Court has consistently held that the commerce clause "does not call for mathematical exactness nor for the rigid application of a particular formula; only if the resulting valuation is palpably excessive will it be set aside." *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. at 455 (quoting *Northwest Airlines, Inc. v. Minnesota*, 322 U.S. 292, 325 (1943) (Stone, C.J., dissenting)). *See Hellerstein, State Taxation Under the Commerce Clause: An Historical Perspective*, 29 *VAND. L. REV.* 335, 347 (1976).

ronmental and other externality costs referred to in *Arizona Public Service*.²⁵¹

Unfortunately, the Court has not yet provided an adequate standard for measuring costs to the state and determining whether a tax is excessive in relation to those costs. Although the “benefits” and “opportunities” language that the Court has adopted from the nexus cases may be a sufficient basis for applying the nexus test, which requires only minimum contacts, it is not helpful in applying the fair-relationship-to-services element of *Complete Auto*. The precise definition of the opportunities, benefits, and services that may be included in the fair relationship equation and how those factors must be measured and weighed will require further clarification through judicial resolution of future cases.²⁵² However it is ultimately defined, the fair-relationship-to-services requirement promises to be the determinative factor in future resource severance taxation cases.²⁵³

²⁵¹ It is interesting to note that when Congress legislates under the commerce clause, the Court gives great deference to the reasonableness of congressional findings that the regulated activity affects commerce. *See Heart of Atlanta Motel, Inc. v. United States*, 379 U.S. 241 (1964). If the Court accorded a similar deference to state legislative findings, the difficulty of determining the reasonableness of replacement costs would be greatly diminished. *Cf. Lindsley v. Natural Carbonic Gas Co.*, 220 U.S. 61 (1911) (in reviewing a legislative classification attacked as denying equal protection, the Court will assume the existence, at the time the law was enacted, of any reasonably conceivable state of facts that would support the classification).

²⁵² How the federal and state interests should be characterized and weighed in the fair-relationship-to-services equation depends a great deal on who is speaking. Representatives of the energy-rich states focus on the need for the tax to avoid the boom-bust cycle and to pay for severe environmental costs, other externality costs imposed by the industry, and the loss of a nonrenewable resource. On the other hand, representatives of consuming states, where higher fuel prices are in part attributable to increased severance taxes, expound the various federal interests: the policies of free trade and open economy that underlie the commerce clause, *see* text accompanying notes 18–25 *supra*, the need to prevent profiteering by resource-rich states at the expense of consuming states, *see* note 26 *supra*, and the conflict between higher extractive taxes and national energy policy during the current energy crisis. *See* note 259 *infra*.

While the federal and state interests can easily be postulated in the extreme, the resolution of any given case will require a delicate weighing of the reasonable costs incurred by the state against the quantum of those costs that can be fairly borne by the interstate market. Striking that balance will be the subject of a subsequent article by the authors. *See* note 253 *infra*.

²⁵³ Several issues arise when the fair-relationship-to-services element of *Complete Auto* is viewed as the central standard against which the amount of a tax is to be judged. The most critical of these issues are the following:

- (1) What kinds of costs to the state justify imposing a resource tax?
- (2) How may a state legitimately measure those costs?
- (3) What standard of review should courts apply to state legisla-

VI

THE SPECTER OF CONGRESSIONAL PREEMPTION

This Article thus far has focused on the negative implication of the commerce clause, which operates through the force of judicial opinions to restrain state regulation of commerce in the absence of congressional action. However, as national energy problems grow more complex and require greater federal involvement, it becomes more likely that Congress will exercise its affirmative commerce power to preempt state resource taxes.²⁵⁴ Rooted in the supremacy of federal law,²⁵⁵ the doctrine of preemption precludes state power to act when (1) the state action conflicts with federal law or (2) a federal legislative scheme is meant to occupy the field.²⁵⁶

A. Conflict Preemption

Conflicts between state and federal law can be either direct or indirect. Indirect conflict occurs when the state law frustrates the policies and objectives of the federal law.²⁵⁷ The preemption test in these circumstances requires an in-depth exploration of the entire federal statutory scheme to determine whether the state law significantly impedes it.²⁵⁸ Thus, if it can be demonstrated that there is a clear federal policy to encourage production of particular energy-producing resources and that a particular state tax or regulation would undermine that federal policy, then the preemption doctrine will come into play.²⁵⁹

tive determinations of the amount of those costs?

(4) To what extent is the state's decisionmaking process relevant to the result reached?

These and other aspects of the fair-relationship-to-services standard, only touched upon here, will be explored in a later article by the authors.

²⁵⁴ See generally Note, *The Increasing Conflict Between State Coal Severance Taxation and Federal Energy Policy*, 57 TEX. L. REV. 675, 689-90, 693-94 (1979); Note, *supra* note 5, at 354-57, 361-63 (1980).

²⁵⁵ U.S. CONST. art. VI, § 2.

²⁵⁶ L. TRIBE, *supra* note 17, § 6-23, at 377. See generally Note, *Pre-emption as a Preferential Ground: A New Canon of Construction*, 12 STAN. L. REV. 208 (1959).

²⁵⁷ See, e.g., *City of Burbank v. Lockheed Air Terminal, Inc.*, 411 U.S. 624 (1973) (local control of take-off hours conflicts with the objectives of the Federal Aeronautics Act); *Nash v. Florida Indus. Comm'n*, 389 U.S. 235 (1967) (state law denying unemployment benefits to persons unemployed because of labor disputes frustrates enforcement of National Labor Relations Act).

²⁵⁸ If the state law merely supplements and does not undermine federal efforts, the Court will allow it to stand. See, e.g., *Colorado Anti-Discrimination Comm'n v. Continental Air Lines, Inc.*, 372 U.S. 714 (1963).

²⁵⁹ A state tax on resources mined on federal land under federal leases raises special preemption problems under the property clause, U.S. CONST. art. IV, § 3, cl. 2, that are not presented when the resources are mined on private or state land. Arguably, under *Kleppe v. New Mexico*, 426 U.S. 529 (1976), any state

Cases of direct conflict present more clear-cut examples of preemption,²⁶⁰ but even they require some degree of statutory interpretation. *Arizona Public Service Co. v. Snead*²⁶¹ is a classic illustration of the kind of statutory interpretation used to determine whether a direct conflict exists. In *Arizona Public Service*, New Mexico argued that the federal act did no more than prohibit state taxes that would be invalid under the negative implication of the commerce clause.²⁶² Because New Mexico's tax on electrical energy arguably did not violate the commerce clause,²⁶³ the state would have had the Court conclude that the tax did not conflict with the federal act. The Court, however, after a thorough review of the federal statute and its legislative history, found that it was not merely coextensive with the commerce clause.

tax that frustrates the policy of a federal law enacted under the property clause violates the supremacy clause, U.S. CONST. art. VI, § 2.

Indeed, the coal companies in *Commonwealth Edison Co. v. State*, 37 Mont. St. Rep. 1192, 615 P.2d 847, *prob. juris. noted*, 101 S. Ct. 607 (1980) (No. 80-581), have argued that the legislative history behind the federal statutory scheme for issuing leases for mining coal on federal lands answers the question of who should get the "economic rents" that necessarily flow from the extraction of the coal. They contend that Congress decided that the federal government should get those rents through its coal leases. For agreeing to this compromise, the states would get a share of all federal royalties. Therefore, the argument goes, the federal statutory scheme precludes state taxation of coal mined under federal leases. *See* Federal Coal Leasing Amendments Act of 1975, Pub. L. No. 94-377, § 9, 90 Stat. 1090 (codified at 30 U.S.C. § 191 (1976)). The Montana Supreme Court, 37 Mont. St. Rep. at 1211, 615 P.2d at 862, rejected this argument, citing the provision of the Mineral Lands Leasing Act that

[n]othing in this chapter shall be construed or held to affect the rights of the States or other local authority to exercise any rights which they may have, including the right to levy and collect taxes upon improvements, output of mines, or other rights, property, or assets of any lessee of the United States.

30 U.S.C. § 189 (1976). The Montana court also relied on the United States Supreme Court decision in *Mid-Northern Co. v. Montana*, 268 U.S. 45 (1925), which had interpreted this provision to allow a one percent state levy on the gross value of oil produced in Montana. 37 Mont. St. Rep. at 1211-12, 615 P.2d at 862-63.

In addition to the policy behind the federal coal leasing scheme, the plaintiff companies invoked a federal policy (developed from a number of statutes) to encourage the development of federal coal. *Id.* at 1207, 615 P.2d at 859. Needless to say, if such a policy could be shown to be substantially frustrated by the Montana tax, preemption considerations would loom large. The Montana Supreme Court did not reach this issue, however, because it failed to discern any federal policy to encourage the development of western coal. *See id.* at 1208-09, 615 P.2d at 860-61.

²⁶⁰ *See* *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963).

²⁶¹ 441 U.S. 141 (1979).

²⁶² *Id.* at 149.

²⁶³ *See* Note, *supra* note 5, at 347-54.

"[T]he provision clearly operates, we think, to carry out the expressed intent of the Senate to invalidate the New Mexico tax."²⁶⁴

The Court's careful scrutiny of the federal statute in *Arizona Public Service* illustrates what Professor Tribe calls the "clear statement requirement," a corollary to the conflict preemption doctrine. In a series of cases striking down the extension of federal criminal jurisdiction under the commerce clause,²⁶⁵ Professor Tribe finds the principle that "unless Congress conveys its purpose clearly, it will not be deemed to have significantly changed the federal-state balance."²⁶⁶ This clear statement requirement, argues Professor Tribe, can have the effect of limiting a given exercise of congressional commerce power when neither the statutory language nor the legislative history clearly states an intent to preempt the state law in question.²⁶⁷

In *Arizona Public Service*, the Court found in the legislative history a clear congressional consensus to void the New Mexico tax on electrical energy.²⁶⁸ Such a consensus, however, may be difficult to achieve for other kinds of resource taxation.²⁶⁹ For example, the recent congressional debate over increased coal severance tax rates in the western states²⁷⁰ suggests that even if Congress attempted to limit coal sever-

²⁶⁴ 441 U.S. at 149.

²⁶⁵ *United States v. Enmons*, 410 U.S. 396 (1973); *United States v. Bass*, 404 U.S. 336 (1971); *Rewis v. United States*, 401 U.S. 808 (1971); *United States v. Five Gambling Devices*, 346 U.S. 441 (1953) (plurality opinion) (Jackson, J.); see L. TRIBE, *supra* note 17, § 5-8, at 243 n.3.

²⁶⁶ L. TRIBE, *supra* note 17, § 5-8, at 243 (quoting *United States v. Bass*, 404 U.S. 336, 349 (1971)).

²⁶⁷ *Id.* § 5-8. The clear statement requirement is derived from cases construing statutes that use commerce clause authority to control noneconomic conduct. See cases cited in note 265 *supra*. Arguably, it is less applicable to congressional action aimed directly at controlling commercial matters.

²⁶⁸ Although the statute on its face was ambiguous, the Court found that the Senate floor debate was explicit. 441 U.S. at 148 (citing 122 CONG. REC. 24,324-29 (1976)). Additionally, the bill was amended specifically "to allay the concerns of Senators from States with [taxes] somewhat similar" to New Mexico's. *Id.* at 148.

The concurring justices in *Arizona Public Service* did not agree that the legislative history clearly evidenced a preemptive intent. Nevertheless, they felt constrained to presume that the federal law went beyond the negative implications of the commerce clause.

[I]t may be unrealistic to assume automatically that Congress never passes a "sterile" law, in the sense that the provision does no more than the Constitution would have done had Congress never enacted the law. But, in my view, the laws enacted by Congress certainly are entitled to a presumption to that effect.

Id. at 151-52 (Rehnquist & White, JJ., concurring).

²⁶⁹ Perhaps a clear legislative statement was possible in *Arizona Public Service* because the statute singled out the New Mexico tax and thus permitted a coalition of all against one. See note 268 *supra*.

²⁷⁰ There are at least two bills before Congress that seek to limit resource

ance taxation, the differing interests within any coalition formed to adopt such legislation would prevent it from expressing a clear congressional purpose. In that event, the clear statement principle could operate to preclude effective federal legislative intervention.

B. Occupation-of-the-Field Preemption

Occupation-of-the-field preemption is less likely than conflict preemption to invalidate state resource taxes. This kind of preemption occurs only when Congress has clearly declared an intent to exercise *exclusive* control over the subject matter, or when the nature of the regulated subject matter mandates an inference that Congress so intended.²⁷¹ The requirement of clear congressional intent to occupy the field will be particularly adhered to when the field is one in which the states historically have operated.²⁷²

Because resource taxation is an area historically left to exclusive state control, it is unlikely to be occupied by federal law.²⁷³ An exception to this general observation, however, is the taxation of nuclear power resources, an area replete with potentially preemptive federal law.²⁷⁴ With its national defense overtones, the field of nuclear power arguably requires exclusive federal control. Indeed, the Atomic Energy Act has been read to provide for exclusive federal regulation of radiation hazards and thus to preempt state nuclear waste laws.²⁷⁵ If federal occupation of the nuclear field encompasses the waste disposal at the end of the nuclear cycle, its extension to uranium mining at the beginning of the cycle is not without logic.²⁷⁶

severance taxes to 12.5%. Those bills are a direct response to Montana's 30% severance tax on coal. Wall St. J., Mar. 26, 1980, at 14, col. 1. In the current congressional debate over increased coal severance taxes, there is at least some recognition that a federally mandated ceiling on severance taxes would implicate the production and processing taxes of other states. As Montana Senator Max Baucus noted in his testimony before the House Commerce and Energy subcommittee: "If you want your state's taxes limited by Congress, then go ahead and pass this bill. It will be the opening shot of the war between the states." Albuquerque J., Mar. 29, 1980, § B, at 1.

²⁷¹ Florida Lime & Avocado Growers v. Paul, 373 U.S. 132, 142 (1963). If the Court finds that Congress intended to occupy the field, then *no* state regulation of the field will be tolerated "no matter how well [it] comport[s] with substantive federal policies." L. TRIBE, *supra* note 17, § 6-25, at 384.

²⁷² "[T]he historic police powers of the States [are] not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947).

²⁷³ For example, in the Natural Gas Policy Act of 1978, Congress was careful to protect state severance taxation from control by the pricing provisions of the law. See Natural Gas Policy Act of 1978, § 110, 15 U.S.C. § 3320 (Supp. III 1979).

²⁷⁴ See, e.g., Atomic Energy Act of 1954, 42 U.S.C. §§ 2011-2282 (1976 & Supp. III 1979).

²⁷⁵ Northern States Power Co. v. Minnesota, 447 F.2d 1143 (8th Cir. 1971), *aff'd mem.*, 405 U.S. 1035 (1972).

²⁷⁶ If state taxation or control of uranium mining were to severely hamper

C. Limits of the Preemptive Power of Congress

As the specter of congressional preemption of state resource taxes looms larger, the states may turn to the recently revitalized notion that state sovereignty provides an inherent limitation on the exercise of congressional power under the commerce clause. In *National League of Cities v. Usery*,²⁷⁷ that rationale was, for the first time since the New Deal, applied to limit the congressional commerce power.²⁷⁸ The Court in *National League of Cities* drew upon the principle of dual sovereignty,²⁷⁹ as well as the tenth amendment doctrine of reserved states' rights,²⁸⁰ to hold that Congress could not use its commerce clause au-

nuclear power production and consequently lead to the enactment of federal statutes, direct conflict preemption could even come into play.

²⁷⁷ 426 U.S. 833 (1976).

²⁷⁸ A number of earlier cases had relied on state sovereignty to limit other constitutional powers of Congress. *See, e.g.*, *Helvering v. Gerhardt*, 304 U.S. 405, 419 (1938) (federal taxing power does not extend to those activities "indispensable to the maintenance of a state government") (dictum); *Coyle v. Smith*, 221 U.S. 559 (1911) (power to admit new states does not authorize Congress to tell a state where to locate its capital).

National League of Cities, however, is the only case since the 1937 shift in the Court to invalidate an act of Congress on commerce clause grounds. Between the turn of the century and 1937, the Supreme Court struck down eight federal acts as exceeding the limits of the commerce power. *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936) (Bituminous Coal Conservation Act); *Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935) (National Recovery Act); *Railroad Retirement Bd. v. Alton R.R.*, 295 U.S. 330 (1935) (Railroad Pension and Retirement Act); *Hammer v. Dagenhart*, 247 U.S. 251 (1918) (child labor laws); *Keller v. United States*, 213 U.S. 138 (1909) (act making it a felony to harbor alien prostitutes); *Adair v. United States*, 208 U.S. 161 (1908) (act making it a crime to discharge employee for membership in a union); *The Employers' Liability Cases*, 207 U.S. 463 (1908) (Employers' Liability Act); *In re Heff*, 197 U.S. 488 (1905) (act prohibiting sale of liquor to Indians).

The doctrinal shift that occurred in 1937 is explained in Stein, *The Commerce Clause and the National Economy*, 59 HARV. L. REV. 645 (1946). *See also* note 47 *supra*.

²⁷⁹ 426 U.S. at 852. The principle of dual sovereignty developed during the period from *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1 (1824), until enactment of the Interstate Commerce Act in 1887. Act of Feb. 4, 1887, ch. 104, 24 Stat. 379 (current version at 49 U.S.C. §§ 10,101-11,916 (Supp. III 1979)). During this period, the Supreme Court rarely reviewed federal action under the commerce clause, L. TRIBE, *supra* note 17, § 5-4, at 233, and its decisions dealing with the limits of the clause "reflect inconsistent doctrinal themes." *Id.* at 233 n.6. Some of the pre-1887 decisions, however, do articulate a principle of dual sovereignty that provides some external limitation on the congressional commerce power. *See, e.g.*, *United States v. DeWitt*, 76 U.S. (9 Wall.) 41, 43-44 (1870) (the federal commerce power "has always been understood . . . as a virtual denial of any power to interfere with the internal trade and business of the separate States").

²⁸⁰ 426 U.S. at 842-43. The tenth amendment rationale of *National League of Cities* was further developed in *Virginia Surface Mining & Reclamation Ass'n v. Andrus*, 483 F. Supp. 425 (W.D. Va.), *prob. juris. noted*, 101 S. Ct. 67 (1980)

thority to extend federal wage and hour laws to state employees.²⁸¹ Although the Court acknowledged that the wage and hour laws were “undoubtedly within the scope of the Commerce Clause,”²⁸² it found that the application of those laws to *state* employees would so encroach on the states’ decisions about how to allocate their financial resources and provide services to their citizens that it would “impermissibly interfere with [their] integral governmental functions.”²⁸³

The Court’s broad language in *National League of Cities* provides a strong argument against federal preemption of state severance taxes. Many of the resource-producing states depend heavily on severance taxation to fund their essential governmental activities. Arguably, a

(Nos. 79-1538 & 79-1596). There, the court acknowledged that the Surface Mining Control and Reclamation Act of 1977, 30 U.S.C. §§ 1201-1328 (Supp. III 1979), was within the scope of the commerce power, but struck it down as transcending the constitutional barrier imposed by the tenth amendment.

Relying on *National League of Cities*, the court drew a distinction between the use of the commerce power to regulate private activity and its use to regulate the states as states. 483 F.Supp. at 432. The Court invalidated the Act because it found that there is a significant impact on the governmental bodies involved: through forced relinquishment of state control of land use planning; through loss of state control of its economy; and through economic harm, from the expenditure of state funds to implement the act and from destruction of the taxing power of certain counties, cities, and towns.

Id. at 435. The case is now on appeal and, if affirmed, could bolster states’ tenth amendment arguments against any congressionally imposed limitation on their severance taxes. *See also* *Indiana v. Andrus*, 501 F. Supp. 452 (S.D. Ind.), *prob. juris. noted*, 101 S. Ct. 67 (1980) (No. 80-231).

²⁸¹ “We hold that insofar as the challenged amendments operate to directly displace the States’ freedom to structure integral operations in areas of traditional governmental functions, they are not within the authority granted Congress by Art. I, § 8, cl. 3.” 426 U.S. at 852.

²⁸² *Id.* at 841.

²⁸³ *Id.* at 851. *National League of Cities* explicitly states that when a federal action “impairs the States’ integrity,” *id.* at 843 (quoting *Fry v. United States*, 421 U.S. 542, 547 n.7 (1974)), forces “relinquishment of important governmental activities,” *id.* at 847, “interfere[s] with traditional aspects of state sovereignty,” *id.* at 849, or “force[s] directly upon the States [federal] choices as to how essential decisions regarding the conduct of integral government functions are to be made,” *id.* at 855, that action impermissibly violates the principles of federalism and the tenth amendment.

In a ringing dissent, Justice Brennan viewed the opinion as a repudiation of the fundamental principle “that the Constitution contemplates that restraints upon exercise by Congress of its plenary commerce power lie in the political process and not in the judicial process.” *Id.* at 857. Even Justice Blackmun, while concurring in the judgment, indicated his difficulty with the broad implications of the opinion. He read the opinion, however, as adopting “a balancing approach, [which] does not outlaw federal power in areas such as environmental protection, where the federal interest is demonstrably greater and where state facility compliance with imposed federal standards would be essential.” *Id.* at 856.

federally imposed ceiling on severance taxes would impair those states' fiscal integrity and "force [a] relinquishment of important governmental activities"²⁸⁴ far more than the minimum wage requirements struck down in *National League of Cities*.²⁸⁵

Thus far, however, *National League of Cities* has done nothing to upset the balance of federal-state power in commerce clause adjudication.²⁸⁶ The Court's failure to develop the principles of *National League of Cities* in subsequent state taxation cases may undercut its viability. Although *Complete Auto Transit* and *Washington Stevedoring* both upheld state taxes against commerce clause challenges,²⁸⁷ the Court failed even to consider the principles of state sovereignty it had articulated in *National League of Cities*. Instead, it announced a balancing principle for weighing state tax schemes against the burdens they impose on commerce. Thus, *National League of Cities* notwithstanding, if Congress makes a judgment that severance taxes above a certain level unreasonably interfere with interstate commerce and clearly states its intent to invalidate those taxes, the Court almost surely will give effect to the congressional action.²⁸⁸

²⁸⁴ *Id.* at 847.

²⁸⁵ See *Indiana v. Andrus*, 501 F. Supp. 452 (S.D. Ind.), *prob. juris. noted*, 101 S. Ct. 67 (1980) (No. 80-231); *Virginia Surface Mining & Reclamation Ass'n v. Andrus*, 483 F. Supp. 425 (W.D. Va.), *prob. juris. noted*, 101 S. Ct. 67 (1980) (Nos. 79-1538 & 79-1596).

²⁸⁶ See, e.g., *Arizona Pub. Serv. Co. v. Snead*, 441 U.S. 141 (1979). *National League of Cities* was virtually ignored in *Massachusetts v. United States*, 435 U.S. 444 (1978), which upheld a federal tax on all civil aircraft as applied to state-owned helicopters used for police functions. See *id.* at 456 & n.13.

The *National League of Cities* argument has been raised, however, in an action by gas-producing states to strike down various provisions of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (Supp. III 1979). See *Oklahoma v. Federal Energy Regulatory Comm'n*, 494 F. Supp. 636 (W.D. Okla. 1980). Quoting from *National League of Cities*, plaintiffs alleged that the Act "force[s] directly upon the States its federal choices as to how the essential decisions regarding the conduct of integral governmental functions are to be made and impair[s] the States' ability to function effectively within the federal system." Complaint at 7-8 (quoting 426 U.S. at 855). The court rejected this argument because (1) it did not feel that the power to tax gas produced and sold intrastate was the type of integral governmental function that *National League of Cities* was referring to, and (2) the plaintiffs had failed to make a sufficient factual showing of the Act's financial impact on the state's ability to structure its integral governmental operations. 494 F. Supp. at 656-57.

²⁸⁷ See text accompanying notes 163-70 *supra*.

The Court in *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980), relied in part on *National League of Cities* considerations in upholding a state preference to in-state purchasers of state-owned cement. See *id.* at 438-39. The dissent in *Reeves* would rely on *National League of Cities* only as authority for "the power of [state] governments to supply their own needs" as opposed to state participation in "the private market . . . for the advantage of its private citizens." *Id.* at 450 (Powell, J., dissenting).

²⁸⁸ If Congress seeks to eliminate *all* severance taxes, however, it will cripple

CONCLUSION

The formalistic delineation of the commerce clause in the pre-New Deal era gave way to the modern balancing approach largely because the earlier formalism did not adequately resolve the more difficult commerce clause questions created by the growing complexities of modern society. The irrelevance of the *Heisler* severance-precedes-commerce analysis to the modern problems that surround our national energy policy is a classic example of the failure of the old devices. Issues that were well settled on the legitimate-state-control side of the ledger in the 1920's have shifted to the national-interest side of the ledger today.

As energy development assumes greater national importance, state resource taxes will come under closer commerce clause scrutiny. Because of the national importance of domestic energy development, state resource taxation should no longer be protected from commerce clause scrutiny by the severance-precedes-commerce formula. If the tax on the privilege of doing interstate business examined in *Complete Auto* and the tax on stevedoring at issue in *Washington Stevedoring* must be "fairly related to the services provided by the State,"²⁸⁹ then taxes on the extractive process should meet the same standard.

the self-governing ability of states that depend heavily on those taxes, and *National League of Cities* will certainly come into play to preclude such a law.

²⁸⁹ *Complete Auto Transit, Inc. v. Brady*, 430 U.S. at 279.

