Tax Incentives Survive U.S. Supreme Court Review

Attracting new businesses to Vermont is an important goal to many in the state. Businesses choose to locate in Vermont for a variety of reasons. Some pick the state for its natural beauty and some because of its well-educated work force. Sometimes, however, more incentives are needed to attract businesses, especially when one considers that nearly every other state provides some sort of tax incentive to attract new businesses to their states. In 1998, the Vermont Legislature responded to calls from tax-incentive proponents by creating the Economic Advancement Tax Incentive Program (EATI). The program provides tax incentives to businesses that locate or expand their operations in Vermont. Additionally, many municipalities enter into tax stabilization agreements or provide other incentives to encourage businesses to locate and remain in their communities.

This month, the Supreme Court decided a case involving an Ohio tax incentive that is strikingly similar to the tax incentives found in Vermont's EATI program. In the case, *Daimlerchrysler Corp. v. Cuno*, the Court reviewed an Ohio tax credit that benefited manufacturers that located and/or installed new equipment at locations in Ohio communities. Several taxpayers challenged the tax credits under the Commerce Clause of the United States Constitution. The taxpayers claimed that the tax credits violated the Commerce Clause by providing an unfair advantage to companies that locate in Ohio and by encouraging companies to move from other states to Ohio. The Sixth Circuit agreed with the taxpayers and found the tax credits to be unconstitutional.

On appeal, the U.S. Supreme Court avoided the issue by ruling on procedural grounds. The Court held that the taxpayers did not have standing to sue Ohio under the Commerce Clause. Had the Supreme Court affirmed the lower court's decision, the tax incentive programs in many states, including Vermont, would have been called into question.

Standing is a requirement imposed on those who wish to gain access to courts. Courts require standing in an attempt to refine who has an interest in a case. Essentially, the court is deciding if someone is the proper person to bring a matter in front of the court. While the requirement for standing to sue in federal court cannot be found explicitly in the text of the Constitution, the Court has ruled that standing is implicitly required based on the constitutional limitation on the federal judiciary to only hear "cases" and "controversies." The Court requires a potential plaintiff to demonstrate three elements in order to establish standing in a federal court: (1) the plaintiff must allege a personal injury; (2) the injury is fairly traceable to the defendant's conduct; and (3) that a favorable court decision is likely to redress the injury.

While the issue of standing may seem complicated and the reasons for having the requirement obscure, a simple example may serve to illustrate the policy behind the rule. Suppose a Vermont landowner negligently spills a toxic substance onto a neighbor's land, making it uninhabitable. A third landowner lives in California. If one would have to choose between the Vermont landowner and the California landowner, most would logically say it is the second Vermont landowner who should be allowed to sue the negligent Vermont landowner. The Vermont landowner has a greater stake in the outcome of the case and incurred an injury that is traceable to the defendant landowner's act. This requirement of standing is based on the logical choice between who should be able to sue and who should not.

In the *Daimlerchrysler* case the taxpayers attempted to establish standing by arguing that tax credits drained revenue from the state, which led to the taxpayers bearing a disproportionate tax burden. The Court rejected this argument. Instead, they found that the taxpayers' supposed injuries were too speculative. First, the program may not result in a net loss of tax dollars as the taxpayers claimed. The goal of the program was to increase tax dollars by stimulating growth, and even if there was a decrease in revenue, there was no evidence that the taxpayers paid more or less money into the state coffers because of the tax credit. Since the taxpayers did not establish a discrete injury that was traceable to the defendant's action, they did not have standing to sue.

The practical effect of the decision is to limit the ability of people to challenge tax incentives on Commerce Clause grounds. The only people who may be able to establish standing in federal court, in order to challenge these incentives, are the people least likely to do so: the businesses who benefit from the tax incentives and other states which likely have similar programs.

The opinion essentially leaves two options for taxpayers dissatisfied with state or local governments giving tax breaks to business. A taxpayer can try to challenge the tax incentives in state courts or use the political process to spur legislative changes. For now, the Vermont Economic Advancement Tax Incentive Program is safe from constitutional challenges.

Municipal governments should note one final distinction. The tax credit in the *Daimlerchrysler* case was a *state* tax incentive. Even though the municipal government in Ohio could also assign tax credits to businesses, both the state and local tax credits derived from the same state tax law. The case also included a municipal property tax exemption separate from the state tax incentive program. The Sixth Circuit ruled that the property tax exemption was constitutional and the Supreme Court declined to hear that portion of the case. This distinction is of some significance. The federal courts treat the standing issue differently, depending on the level of government involved. Under the "municipal taxpayer standing" rule, federal courts have been more likely to find a taxpayer established standing when suing a municipality concerning a strictly municipal tax. The courts recognize that taxpayers have a more direct stake in how their local tax dollars are collected and spent.

Under the "municipal taxpayer standing" rule, the taxpayers would likely have been able to establish standing to sue the municipality concerning the municipal property tax exemption. While this does not mean that local tax exemptions, which benefit businesses, will be found unconstitutional (in fact the Sixth Circuit actually upheld the local property tax exemption), municipalities should note the increased scrutiny that may be given to the tax exemptions that they provide.

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