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Louisiana Supreme Court Rejects Dormant Commerce Clause Challenge to State's *Ad Valorem* Tax Scheme

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In a decision with sweeping implications for interstate pipeline companies that do business in Louisiana, the Louisiana Supreme Court recently upheld the constitutionality of the state's *ad valorem* tax scheme, which requires interstate pipeline companies to pay tax at a 10 percent greater rate than certain intrastate pipeline companies. Despite the apparent facial discrimination against interstate pipeline companies embodied by the scheme, the Louisiana Supreme Court reversed two lower-court decisions finding that the disparity treatment violated the dormant aspect of the Commerce Clause, reasoning that imposition of the higher tax rate turned not on the interstate or intrastate character of the companies, but on how the companies were regulated. The fact that all industry operators would be regulated so as to be subject to a higher rate did not amount to facial discrimination. The decision raises interesting and unanswered questions about the proper scope of the facial-discrimination inquiry in a Dormant Commerce Clause challenge to a purportedly discriminatory state tax.

Louisiana's *Ad Valorem* Tax Scheme

The parameters of Louisiana's *ad valorem* tax scheme are laid out in the Louisiana Constitution. Properties classified as "public service properties" are taxed at the rate of 25 percent of their fair market value, whereas property classified as all "other property" is taxed at the rate of 15 percent. La. Const. Art. VII, § 18(B). The Louisiana Legislature, acting under authority granted by the Constitution, defined "public service properties" as "immovable, major movable, and other movable property owned or used but not otherwise assessed in this state in the operations of each . . . *pipeline company*. . . ." La. R.S. 47:1851(M) (emphasis added). "Pipeline company," in turn, is defined as:

> [A]ny company that is engaged in the business of transporting oil, natural gas, petroleum products, or other products within, through, into, or from this state, and which is regulated by (1) the Louisiana Public Service Commission . . . , (2) the Interstate Commerce Commission, or (3) the Federal Power Commission, as a "natural gas company" under the Federal Natural Gas Act, 15 U.S.C. §§ 717–717w, because that person is engaged in the transportation of natural gas in interstate commerce, as defined in the Natural Gas Act.

La R.S. 47:1851(K). Under federal law, all interstate natural gas pipeline companies are regulated by the Federal Energy Regulatory Commission ("FERC"),[1] making all interstate pipeline companies that do business in Louisiana invariably "public service properties" subject to the state's higher 25 percent *ad valorem* tax. But under Louisiana law, only those intrastate pipeline companies that sell to local distributing systems are rate-regulated by the Louisiana Public Service Commission, La. R.S. 30:551(A), meaning only those intrastate companies are "public service properties" subject to the heightened tax; assets held by all other intrastate pipelines are considered "other property" subject to the 15 percent *ad valorem* tax under La. Const. Art. VII § 18(B). Accordingly, the Louisiana *ad valorem* tax scheme, on its face, requires all interstate pipeline companies to pay a 25 percent tax, whereas intrastate companies may opt out of the tax by strategically structuring their business operations.

The Louisiana Supreme Court's Decision

Several interstate pipeline companies raised a Dormant Commerce Clause challenge to the *ad valorem* tax scheme, contending that the scheme impermissibly discriminates against interstate commerce. Under the U.S. Supreme Court's seminal decision in *Amerada Hess Corp. v. Director, Division of Taxation, New Jersey Department of the Treasury*, a state tax discriminates against interstate commerce if it (1) is facially discriminatory; (2) has a discriminatory intent; or (3) has the effect of unduly burdening interstate commerce. 490 U.S. 66, 75 (1989).

Both the trial court and the Louisiana Court of Appeals found that the *ad valorem* tax scheme facially discriminates against interstate commerce. The Louisiana Supreme Court disagreed. According to that court, "Regulatory status is the factor that determines what is considered a 'pipeline company' [subject to the 25 percent tax], not interstate or intrastate character . . . ." *Transcontinental Gas Pipeline Corp. v. Louisiana Tax Commission*, ___ So. 3d ___ (La. 2010). The court reasoned that the *ad valorem* tax scheme did not grant a benefit to intrastate companies over interstate companies; the scheme applies equally to both in-state and out-of-state companies because "any rate-regulated pipeline company transporting gas in [Louisiana]" is subject to the 25 percent tax. *Id*.

While the court acknowledged that the scope of FERC's regulation forbids interstate companies from ever taking advantage of the lesser 15 percent tax, it found this to be "an incidental effect of the classification due to preemption of federal law, and not a patent facial discrimination against interstate commerce." *Id*. While the pipeline operators also mounted attacks on the tax's operation, claiming that the different rates and methods of calculation operated to discriminate against interstate commerce, the court found that none of the companies could carry the heavy evidentiary burden of showing that the actual tax rendition was greater under the higher rate, rejecting the companies' argument that different valuation methods—actual valuation and the unit method—would have resulted in the same base of calculation. Because the companies would never be able to prove what actual valuation would have been applied in every individual parish across the state to support such a claim, the standard applied to facial challenge became effectively outcome determination. Accordingly, the Louisiana Supreme Court reversed the court of appeals' decision and upheld the constitutionality of the tax scheme. *Id*.

[1] FERC is the successor to the Federal Power Commission. 15 U.S.C. §§ 717–717z.

What Is "Facial Discrimination" Under the Dormant Commerce Clause?

The court's reasoning raises important questions for interstate taxpayers about the depth of inquiry permissible in a facial challenge to a purportedly discriminatory state tax. The Louisiana Supreme Court cited no precedent for the proposition that a state tax scheme apportioned by regulatory status—or any other determinative proxy—which is itself based on the interstate or intrastate character of companies is beyond the purview of facial discrimination. Rather, the court supported its facial-discrimination analysis exclusively by distinguishing cases where the court had struck down state taxes as facially discriminatory. The thin precedential basis for the Louisiana Supreme Court's decision is not surprising. As commentators have noted, unlike other discrimination jurisprudence law, the precise scope of the facial-discrimination test under *Amerada Hess—i.e.*, how far from the face of a statute a court can look to establish discrimination—is unclear. *See* David S. Day, *The Expanded Concept of Facial Discrimination in the Dormant Commerce Clause Doctrine*, 40 Creighton L. Rev. 497 (2007).

This is not a purely academic issue. Proving that a legislature acted with discriminatory intent can be extremely difficult, and establishing discriminatory effects is both burdensome and costly, as this case showed. Thus, a facial challenge will almost always be the taxpayer's preferred—and perhaps only usable—line of attack.

In other contexts, it is clear that status or characteristics cannot be used as a proxy for discrimination; if they are, the statute or practice will not be immune from a facial attack. For example, courts have found explicit age-based discrimination where a county used a proxy for age—Medicare eligibility—as a basis for differential treatment. *Erie County Retirees Ass'n v. County of Erie, Pa.*, 220 F.3d 193, 215 (3d Cir. 2000). Likewise, an employer could not use gray hair as the basis for differential treatment because the "'fit' between age and gray hair is sufficiently close that they would form the same basis for invidious classification." *McWright v. Alexander*, 982 F.2d 222, 228 (7th Cir. 1992). Similarly, a school's exclusion of a service dog has been held to be "discrimination because of handicap." *Sullivan v. Vallejo City Unified Sch. Dist.*, 731 F. Supp. 947, 958 (E.D. Cal. 1990). "[A]nd no doubt a policy excluding wheelchairs would be such discrimination, even if the stated purpose of the policy were a benign one." *Alexander*, 982 F.2d at 228.

As mentioned, the extent to which this reasoning applies in the context of a Dormant Commerce Clause challenge remains unclear. The Louisiana Supreme Court's recent decision does nothing to clear up that ambiguity.

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