No. 13-657

IN THE

Supreme Court of the United States

MCLANE SOUTHERN, INC.,

Petitioner,

v.

CYNTHIA BRIDGES, SECRETARY OF THE DEPARTMENT OF REVENUE, STATE OF LOUISIANA,

Respondent.

On Petition for Writ of Certiorari to the Louisiana Court of Appeal, First Circuit

REPLY TO BRIEF IN OPPOSITION

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TABLE OF CONTENTS

Page

INTRODUCTION 1

REASON FOR GRANTING THE WRIT 2

The Commerce Clause Does Not Allow States To Tax Goods Distributed By Out-Of-State Wholesalers More Heavily Than Goods Distributed By In-State Wholesalers. 2

A. State Excise Taxes Based On The Price Invoiced To The First Distributor To Send A Product Into The State Discriminate Against Out-Of-State Economic Activity. 2

B. A State Cannot Justify A Discriminatory Excise Tax By Blaming Others For The Discrimination. 6

C. The Issue Warrants This Court's Review. 8

CONCLUSION 10

TABLE OF AUTHORITIES

Page(s)

Cases

Halliburton Oil Well Cementing Co. v. Reily,
373 U.S. 64 (1963) 5, 6

Kraft Gen. Foods, Inc. v.
Iowa Dep't of Revenue & Fin.,
505 U.S. 71 (1992) 6

Lynn Creamery, Inc. v. Healy,
512 U.S. 186 (1994)..10

McLane Minn., Inc. v. Commissioner of Revenue,
773 N.W.2d 289 (Minn. 2009) 8, 9

McLane Western Inc. v. Department of Revenue,
549 U.S. 810 (2006) (order) 8, 9

Mutual Pharm. Co. v. Bartlett,
133 S. Ct. 2466 (2013) 6

Statutes

28 U.S.C. § 1341 10

Colo. Rev. Stat. § 39-28.5-101(2).................................9

Other Authorities

Hellerstein, Jerome R. & Hellerstein, Walter,
State Taxation (2013) 4

The Federalist Papers
(Clinton Rossiter ed., 1961)............................10

INTRODUCTION

Louisiana's brief in opposition never comes to grips with the question presented in the petition: whether States may "tax goods distributed by out-of-state wholesalers more heavily than goods distributed by in-state wholesalers." Pet. i. In particular, Louisiana does not, and cannot, deny that the excise tax at issue here does just that.

Rather, Louisiana defends the tax on the ground that it taxes all goods at the same rate on a tax base determined in the same fashion. As noted in the petition, however, the tax base here shifts in a way that discriminates against interstate commerce. Because the tax is based on the price invoiced to the first distributor to send the product into the State, the tax will necessarily be higher where distribution activities (and the corresponding markup in price) occur out-of-state rather than in-state.

Louisiana can scarcely contest that point, because this case proves it. If McLane moved its distribution facility across the Mississippi River from Mississippi into Louisiana, it would reduce the amount of the Louisiana excise tax. That simple point—which Louisiana does not, and cannot, deny—should be the beginning and the end of this case: this is precisely the sort of discrimination that the Commerce Clause prohibits.

This Court should grant review here to determine the constitutionality of state excise taxes that, like Louisiana's, apply a uniform tax rate to a shifting tax base that discriminates against out-of-state economic activity. Because such taxes have been proliferating in recent years, but have been upheld by the state courts, this Court's review is needed to halt this discriminatory trend.

REASON FOR GRANTING THE WRIT

The Commerce Clause Does Not Allow States To Tax Goods Distributed By Out-Of-State Wholesalers More Heavily Than Goods Distributed By In-State Wholesalers.

A. State Excise Taxes Based On The Price Invoiced To The First Distributor To Send A Product Into The State Discriminate Against Out-Of-State Economic Activity.

Louisiana asserts that the excise-tax scheme at issue here is not unconstitutionally discriminatory because all goods within its scope are "taxed at the same rate and on a tax base determined in the same fashion." Opp. 13. But that assertion begs the key question whether the "fashion" in which Louisiana determines the tax base—*i.e.*, by looking to the price invoiced to the first entity to send the goods into the State—is itself discriminatory. It is, and therefore violates the Commerce Clause.

The Louisiana excise tax at issue here, like similar excise taxes imposed by twenty other States, *see* Pet. 17 n.1, necessarily results in a higher tax on goods that enter the State at a later stage in the distribution process, because the price invoiced for those goods will necessarily be higher at that stage. As Louisiana itself acknowledges, "it is true that, as [a product] passes through a supply chain, [its] ultimate taxable price accumulates the middleman's markups," thereby resulting in a "competitive disadvantage" for goods that are taxed on the marked-up price as opposed to those that are not. Opp. 10. Because the Louisiana excise tax is based on the price invoiced to the first entity to send the goods into the State, it taxes price markups based on out-of-state economic activity but not in-state economic activity. The more distribution activity that occurs out-of-state, the higher the price on which the tax is based. That is why goods sold by McLane from a distribution center in Mississippi are subject to a higher tax than the same goods sold by its competitor Imperial from a distribution center in Louisiana.

Louisiana tries to avoid this straightforward point by asserting that it "*must* tax the actual invoice price paid by … the [first distributor to send the product into the State]." Opp. 8 (emphasis added). That assertion is simply untrue. To the contrary, as noted in the petition, other States base their excise taxes on factors that do not discriminate against out-of-state wholesalers, such as (1) the product's weight, *see* Pet. 19 n.2, (2) the price charged by the manufacturer, *see id.* n.3, or (3) the price charged to a retailer, *see id.* at 20 n.4. Indeed, given that nineteen States base their smokeless-tobacco excise taxes on the manufacturer's invoice price, regardless of subsequent markups in the distribution chain, *see id.* at 19 n.3, Louisiana clearly errs by asserting that "[b]asing a taxpayer's burden on an ancillary transaction that does [not] involve the taxpayer would be novel in the area of transactional and excise taxes." Opp. 6. Excise taxes based on price markups that reflect out-of-state economic activity but not in-state economic activity are a recent phenomenon, and inherently discriminate against interstate commerce by pressuring businesses to move their distribution facilities in-state. *See*, *e.g.*, Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* ¶ 4.14[3][n] (2013).[1]

Louisiana tries to blame the distribution chain for this problem, asserting that "a product [with] a long distribution and supply chain will likely be [at] a competitive disadvantage to one that has … a shorter distribution and supply chain." Opp. 10. But the problem has nothing to do with the number of links in a particular distribution chain; rather, the problem has to do with the number of links in the distribution chain *outside the State*. The Louisiana statute taxes the same product differently even if the same number of "middlemen" are involved in the supply chain, depending on how many of those middlemen are located outside of Louisiana: the more links in the supply chain outside the State, the higher the tax. Once the product enters the State, the base for the excise tax is fixed regardless of how many further steps in the distribution chain, and corresponding markups in the product's price, occur.

For this reason, Louisiana's analogy to a "sales and use tax" is misplaced. Opp. 11. As Louisiana

[1] Louisiana impugns Professor Walter Hellerstein, whose work on state taxation this Court has cited more than a dozen times, by asserting that his treatise "cannot … be considered unbiased" because he supported McLane's efforts to secure review of the Colorado case eight years ago. Opp. 21. The suggestion that the views expressed in the treatise reflect Professor Hellerstein's involvement in that case, rather than vice versa, is both inaccurate and offensive. Louisiana is conspicuously unable to cite *any* commentary supporting the constitutionality of state taxes that vary depending on the point in a distribution chain when a product crosses state lines.

points out, "[t]he retail sales price … reflects an accumulation of markups imposed by middlemen suppliers (called wholesalers) as the product passes through the distribution and supply chain," so that "[t]he fewer middlemen in the chain, the lower the price the retailer charges its customers and the lower the sales tax associated with the sales price." *Id.* But no one is suggesting that there is any inherent constitutional problem with state taxation "on a marked-up price." *Id.* Rather, the problem arises where, as here, States discriminate against interstate commerce by taxing marked-up prices that reflect out-of-state, but not in-state, economic activity. Regardless of whether structured as an excise tax or a sales tax, a discriminatory tax violates the Commerce Clause.[2]

Nor can Louisiana deny that such discrimination violates this Court's holding in *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), that States cannot use a shifting tax base to discriminate against out-of-state economic activity. Louisiana

[2] Louisiana similarly misses the point by asserting that "the high levels of taxation of in-state activity related to the manufacture, sale, and distribution at issue here serves to discourage such activity in Louisiana." Opp. 6. What matters is not whether a particular tax is deemed "high" or "low"—which will invariably depend on the eye of the beholder—but whether it is discriminatory. *Any* tax can be said to discourage the activity being taxed, but this Court has never upheld a *discriminatory* tax on the theory that it discourages such activity. Where, as here, a state tax is based on price markups that reflect out-of-state but not in-state economic activity, distributors will necessarily be pressured to move their distribution activities in-state.

contends that *Halliburton* is inapposite because "Louisiana's tax scheme does not mandate a disparity in the treatment of distributors similar to that addressed in *Halliburton*." Opp. 19. But that is simply not true. As noted above, the Louisiana tax scheme at issue here, like the Louisiana tax scheme at issue in *Halliburton*, "increase[s]" the "tax base" for out-of-state economic activity, 373 U.S. at 70—the more distribution activity that occurs out-of-state, as opposed to in-state, the higher the price on which the tax is based.

B. A State Cannot Justify A Discriminatory Excise Tax By Blaming Others For The Discrimination.

Because Louisiana cannot seriously dispute that its excise tax discriminates against out-of-state wholesalers, it devotes much of its brief to trying to blame others for the discrimination. As an initial matter, Louisiana asserts that McLane's "competitive disadvantage is a product of McLane's decision to purchase smokeless tobacco through a distribution supply chain rather than directly from a manufacturer." Opp. 10-11; *see also id.* at 11 ("[T]he higher tax McLane wishes to avoid is of its own making and a product of its own smokeless tobacco purchasing model, not Louisiana's smokeless tobacco-tax scheme.").

That assertion misses the point. It is axiomatic that a State cannot justify an unconstitutional law by simply alleging that those subject to the law can change their otherwise lawful behavior. *See*, *e.g.*, *Mutual Pharm. Co. v. Bartlett*, 133 S. Ct. 2466, 2477-78 (2013); *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Fin.*, 505 U.S. 71, 78 (1992). Thus, McLane need not alter its "purchasing model" to save the Louisiana tax scheme. And in any event, McLane cannot alter that model: like any other entity engaged in buying, McLane can buy only from an entity engaged in selling. Just as a consumer cannot buy a car from a manufacturer that sells exclusively through dealers, McLane cannot buy smokeless tobacco from a manufacturer that sells exclusively through a dealer. *See* Opp. App. 3-4a. The price invoiced by the dealer invariably includes a markup that reflects the dealer's marketing, distribution, and advertising services, which the manufacturer does not provide.

Similarly unavailing is Louisiana's related argument that the discrimination "is not the result of Louisiana's tax scheme, but is the result of UST Sales' business model." Opp. 17. Although this argument is somewhat inscrutable, Louisiana characterizes UST's decision to spin off its distribution arm from its manufacturing arm as "artificial" and "questionable." Opp. 7, 12, 19. But a State cannot justify a tax that structurally discriminates against out-of-state economic activity by insinuating that a particular out-of-state entity has engaged in some unspecified impropriety—especially where, as here, that entity is concededly unrelated to the taxpayer.

Not surprisingly, thus, the court below did not rely on any such supposed impropriety in upholding the excise tax at issue here. To the contrary, rather than disregarding the distinction between UST-Manufacturing and UST-Sales, the court below acknowledged that "'McLane is correct that calculating the tobacco tax using the price that

McLane pays to UST-Sales, instead of the amount that UST-Sales pays to UST-Manufacturing, has the effect of increasing the amount of the tobacco tax that it pays as the tax-liable distributor.'" App. 11-12a (quoting *McLane Minn., Inc. v. Commissioner of Revenue*, 773 N.W.2d 289, 299 (Minn. 2009); brackets omitted). Beyond this undisputed point, the relationship between UST-Sales and UST-Manufacturing is immaterial.

Louisiana thus errs by asserting that "*[t]he central premise* of McLane's claim is that an earlier sale and purchase of smokeless tobacco between UST Sales and UST Manufacturing … somehow should determine the tax base upon which McLane calculates its smokeless tobacco tax liability." Opp. 5-6 (emphasis added). That was the central premise of McLane's state *statutory* argument, which it lost below and is not pursuing here. McLane's federal *constitutional* argument, in contrast, has nothing to do with UST. Louisiana, not UST, is responsible for the discriminatory taxation at issue here.

C. The Issue Warrants This Court's Review.

Finally, Louisiana contends that this Court's review is unwarranted because this Court in 2006 declined to review a case involving a similar Colorado excise tax. *See* Opp. 5 (citing *McLane Western Inc. v. Department of Revenue*, 549 U.S. 810 (2006) (No. 05-1294) (order denying certiorari). According to Louisiana, "[n]othing of merit factually or legally has changed to justify a different result now." *Id.*

That is not accurate. Although the Colorado case also involved a statute with a shifting tax base, that case differed in a significant way from this one. The

Colorado tax is imposed on the entity that "first receives" the product in-state. Colo. Rev. Stat. § 39-28.5-101(2). Thus, the petitioner in the Colorado case was located *within* the taxing State, and the case did not present the question whether States may tax goods distributed by out-of-state wholesalers more heavily than goods distributed by their in-state competitors. That is, of course, the very question presented here.

In addition, the Colorado petition acknowledged that the issue presented there was then novel, but urged this Court to grant review because the Colorado decision upholding the tax "would provide a template for States to discriminate against interstate commerce by the simple expedient of effectuating such discrimination through a shifting tax base …." Pet. for Cert., *McLane Western*, at 8; *see also id.* at 16 (arguing that review warranted because Colorado's tax "will provide a simple formula for state legislature to enact discriminatory state taxes").

In the eight years since this Court declined to review the Colorado case, the predictions made in that petition have been borne out. As explained in McLane's petition in this case, and not disputed by Louisiana, twenty States impose excise taxes that use a shifting tax base to discriminate against out-of-state economic activity. Since this Court declined to review the Colorado decision, several of those States adopted those statutes, *see* Pet. 17-18 & n.1, and state courts in Minnesota and Louisiana construed their statutes in the same way and upheld them against federal constitutional challenges. *See McLane Minn.*, 773 N.W.2d at 292-300; Pet. App. 6-15a. For this Court now to decline review will not only perpetuate these discriminatory regimes, but also embolden other States to adopt similar regimes either to secure or to neutralize a competitive advantage. *See id.* at 20.

Similarly, in contrast to other federal issues that can percolate in the lower federal courts, the issue presented here cannot. Louisiana does not, and cannot, dispute that the Tax Injunction Act, 28 U.S.C. § 1341, prevents this issue from reaching those courts. Rather, Louisiana insists that "state court decisions on these issues should be respected as it is state courts … that are the courts that face these issues and in turn have great experience resolving such." Opp. 21.

It is no disrespect to the state courts, however, to acknowledge that the Framers gave *this* Court the power to review issues of federal constitutional law decided by those courts. *See* The Federalist No. 82, p. 494 (C. Rossiter ed., 1961) (Hamilton). And few issues so concerned the Framers as the States' natural tendency to discriminate against out-of-state economic activity. *See, e.g.*, *id.*, No. 7, pp. 62-63 (Hamilton); *id.*, No. 11, pp. 89-90 (Hamilton). Accordingly, this Court has long recognized a "duty" to invalidate discriminatory state laws, *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 201 (1994), even in the absence of a conflict among the state courts, *see* Pet. 22 (citing cases). This case calls upon this Court once again to fulfill that duty.

CONCLUSION

For the foregoing reasons, and those set forth in the petition, the Court should grant review.

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