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IN THE
Supreme Court of the United States

OCTOBER TERM, 1992

STATE OF CONNECTICUT, *et al.*,
Plaintiffs,
v.

STATE OF NEW HAMPSHIRE,
Defendant.

On Exceptions to the Final Report of the Special Master

REPLY BRIEF FOR INTERVENORS

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REPLY BRIEF FOR INTERVENORS

This case involves a challenge to the New Hampshire "Tax on Nuclear Station Property" (N.H. Rev. Stat. Ann. Ch. 83-D) and an accompanying credit for payment of that tax against liability for the New Hampshire Business Profits Tax (N.H. Rev. Stat. Ann. Ch. 77-A:5). The Special Master recommended that this Court hold these tax measures, taken together, to be in violation of the Commerce Clause of the United States Constitution, art. I, § 8, cl. 3, and of the provisions of 15 U.S.C. § 391. The Special Master further recommended that this Court award retroactive relief in the form of refunds of the tax paid less any credit taken against liability for business profits taxes. Intervenors [1] urge that the Court adopt the recommendations of the Special Master and, consequently, overrule the exceptions lodged by New Hampshire.

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[1] Intervenor The Connecticut Light and Power Company does not participate in this filing.

STATEMENT

1. *The New Hampshire Tax System.* In 1991 the New Hampshire legislature, endeavoring to increase state revenues, enacted a "Tax on Nuclear Station Property." 1991 N.H. Laws c. 354 (to be codified at N.H. Rev. Stat. Ann. ("RSA"), Chapter 83-D) (the "Seabrook Tax"). The legislature did not just enact a new tax, however; it provided, at the same time, that payment of the Seabrook Tax would be allowed as an offset against liability for a second tax: the New Hampshire Business Profits Tax. 1991 N.H. Laws c. 354.2 (to be codified at RSA ch. 77-A:5, VI).[2] Pursuant to the New Hampshire statutes, any payment of the Seabrook Tax may be taken as a credit, dollar-for-dollar, against tax owed on New Hampshire business profits. The effect of the Seabrook Tax thus varies with respect to each owner, according to the extent of New Hampshire business profits that it earns.

a. *The Seabrook Tax.* The Seabrook Tax is an *ad valorem* tax imposed upon "nuclear station property." The statute defines the property subject to the tax as "the land, buildings, structures, tunnels, machinery, dynamos, apparatus, poles, wires, nuclear fuel and fixtures of all kinds and descriptions used in generating, producing, supplying and distributing electric power or light from the fission of atoms, exclusive of transmission lines." Ch. 83-D:2. As the Special Master noted, "[t]he only nuclear generating station in New Hampshire (and thus the only facility affected by the tax) is the Seabrook Station located in the town of Seabrook, New Hampshire." Final Report 2 n.1. *See* Stip. ¶ 3.2 & 3.3.[3]

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[2] In the legislation imposing the Seabrook Tax, New Hampshire repealed its franchise tax insofar as it applied to sales of electricity. 1991 N.H. Laws c. 354:3.

[3] The Seabrook Nuclear Station, like other facilities generating electricity in New Hampshire, is subject to local property taxes. Final Report 6 n.3; Stip. ¶ 3.3. No statewide property tax is imposed on other generating facilities. Final Report 6 n.4.

The tax is imposed at the rate of 0.64% of the value of the nuclear station property. Ch. 83-D:3. The 1991 Act established a maximum initial value of the Seabrook Station at $3.5 billion, Ch. 83-D:9, but it provided for subsequent valuation by the commissioner of revenue administration. Ch. 83-D:4. "The tax is assessed on each of the joint owners of nuclear station property in proportion to its ownership share." Final Report 7. *See* Ch. 83-D:5. Liability is several, not joint or joint and several. Stip. ¶ 3.5.

b. *The New Hampshire Business Profits Tax.* The State also imposes a tax "upon the taxable business profits of every business organization." Ch. 77-A:2. For a business deriving "gross business profits from business activity both within and without this state," New Hampshire provides that the business should apportion its profits "so as to allocate to this state a fair and equitable proportion of such business profits." Ch. 77-A:3.

The primary method of apportioning business profits is a three-part weighted formula set forth in the statute. Ch. 77-A:3; *see* Final Report 10. According to the formula, an organization doing business both intrastate and interstate must calculate the percentages of in-state property compared to all property, in-state compensation compared to all compensation, and in-state sales compared to all sales. The business then averages the three percentages, after giving added weight to the sales factor, to arrive at the ratio of business profits to be treated as New Hampshire business profits. *See* Final Report 9-10.[4]

The tax rate imposed on the New Hampshire share of business profits is 8 percent. Ch. 77-A:2. As a result of the credit provision, therefore, a Seabrook owner paying $1 million in Seabrook Tax would be able to earn up

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[4] The property percentage and the compensation percentage are added to 1.5 times the sales percentage, and then the resulting sum is divided by 3.5. 1991 N.H. Laws c. 354:7 (to be codified at RSA ch. 77-A:3, II(a)).

to $12.5 million in business profits without incurring additional tax liability—provided, of course, that the business profits were earned in New Hampshire. The credit provision gives assurance that only one tax is due for the activities of owning Seabrook and earning business profits (up to the point that the credit is exhausted), so long as the profits are local and not generated in other States.

The link between the Seabrook Tax and the New Hampshire Business Profits Tax is reaffirmed by another provision of the statute: the Nonseverability Clause. 1991 N.H. Laws c. 354:19. That clause states that "[i]t is the intent of the legislature that sections 1 and 2 of this act [the Seabrook Tax and the credit against Business Profits Tax] be considered a unit and their provisions inseparable." *Id.* It then goes on to provide explicitly that "[i]f any provision of sections 1 and 2 of this act is declared unconstitutional, then sections 1 and 2 and all of their provisions shall be invalid." *Id.*

2. *Operation of the New Hampshire Tax System.* Each of the intervenors owns part of the Seabrook Nuclear Station. *See* Stip. ¶¶ 1.3-1.9. As an owner, each is liable for a *pro rata* share of the Seabrook Tax. Moreover, except for Taunton Municipal Lighting Plant, each is subject to taxation on its business profits in New Hampshire and other States in which it conducts business.[5]

a. *Payments of Seabrook Tax.* The Seabrook Tax was imposed with an effective date of July 1, 1991, and payments for 1991 were limited to one-half of the amount that would be due on an annual basis. Final Report 7. *See* Stip. ¶ 4.1; Ch. 354:21 & 83:D-9. For that six-month period, the Seabrook owners as a whole paid approximately $11.2 million in Seabrook Tax. Final Report

[5] A complete listing of Seabrook owners, and their respective shares of ownership, is set forth in Appendix A of the Final Report and in the Stipulation at ¶¶ 3.6-3.18.

7; *see* Stip. ¶ 4.2.[6] Intervenors' share amounted to $4.26 million (38%). *Id.*

The valuation for 1992 is expected to increase to just under $3.75 billion. Final Report 8; *see* Stip. ¶ 4.3. Based upon that figure, the total Seabrook Tax payments for 1992 amount to approximately $24 million. Final Report 8; *see* Stip. ¶¶ 4.4-4.7. Intervenors' share of that figure would be $9.125 million (38%). *Id.*

The Special Master found that owners of Seabrook are passing on the Seabrook Tax in the wholesale and retail rates charged to their customers. Final Report 8-9 & App. B; *see* Stip. ¶¶ 5.5-5.20. For example, Canal Electric Company has included the Seabrook Tax in the wholesale rate, approved by the Federal Energy Regulatory Commission (FERC), charged to Commonwealth Electric Company and Cambridge Electric Light Company. *See* Final Report App. B; Stip. ¶ 5.6. Those companies, in turn, have included the Seabrook Tax, passed through to them by Canal, in the retail rates charged to their Massachusetts customers, pursuant to approvals given by the Massachusetts Department of Public Utilities in October 1991. *See* Final Report App. B; Stip. ¶¶ 5.7, 5.8. Similarly, New England Power has included the Seabrook Tax, with FERC approval, in wholesale rates charged to various affiliated companies, Stip. ¶ 5.11, which have then passed on the tax to customers in Massachusetts, Rhode Island, and New Hampshire. Final Report App. B; Stip. ¶¶ 5.12-5.14. Montaup has included the Seabrook Tax in wholesale rates, approved by FERC (Stip. ¶ 5.15), to affiliated companies that have passed on the tax to customers in Massachusetts and Rhode Island. Final Report App. B; Stip. ¶¶ 5.16-5.20.[7]

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[6] For simplicity, the figures used in this section are approximate. Exact figures are set forth in the Final Report at Appendix A and in the Stipulation at the indicated paragraphs.

[7] *Amicus curiae* Massachusetts Municipal Wholesale Electric Cooperative ("MMWEC") has been passing through the Seabrook Tax as well. *See* Final Report App. B; Stip. ¶¶ 5.9-5.10.

Other Seabrook owners are passing, or will pass, the Seabrook Tax on directly to retail customers. Taunton Municipal Lighting Plant and the Town of Hudson (Massachusetts) Light and Power Department, neither of which is required to obtain regulatory approval, have included the Seabrook Tax in the calculation of rates charged to customers in Massachusetts. Final Report App. B; Stip. ¶¶ 5.21-5.22. United Illuminating Company received authorization from the Connecticut Department of Public Utility Control to recover the Seabrook Tax in rates effective on January 1, 1993. Final Report 9; Stip. ¶ 5.23.

b. *Use of the Seabrook Tax to Offset Business Profits Taxes.* Each of the Seabrook owners and its affiliated companies—excepting owners exempt from income taxes as governmental entities—is subject to taxation on its business profits. Not only does New Hampshire tax business profits, but Connecticut, Massachusetts, and Rhode Island do as well. Final Report 11-12; Stip. ¶ 2.4. Each State provides that, for multi-state businesses, the tax on business profits should be calculated after apportionment of business profits to reflect the amount of business conducted in that State. Final Report 9-10.

The liability of each Seabrook owner for tax on its overall business profits is directly affected by the credit provision contained in the New Hampshire statute. Because the credit provides an offset only against profits earned locally, the ability of a Seabrook owner to shelter its business profits from taxation depends on the extent to which its profits are earned in New Hampshire. For example, United Illuminating Company will pay approximately $4.2 million in Seabrook Tax for 1992; it thus would be able to earn up to $52.5 million in New Hampshire business profits for 1992 without any additional tax liability.[8] However, given that United Illuminating has

[8] As previously noted, with a dollar-for-dollar credit for the amount paid in Seabrook Tax and a tax rate of 8 percent on business

no sales or employees or property (other than Seabrook) in New Hampshire, virtually all of its $26.4 million in business profits is earned *outside of* New Hampshire—specifically in Connecticut. United Illuminating is able, therefore, to shelter only slightly less than $3.6 million of its profits from taxation, while remaining subject to taxation in other States on the remaining $22.8 million.

Other Seabrook owners, likewise, face higher overall taxation on their business profits solely because they do business in States other than New Hampshire.[9] In 1992 Canal will pay slightly under $850,000 in Seabrook Tax. If Canal conducted a wholly intrastate business within New Hampshire, or otherwise had substantial activities within the State, it could earn as much as $10.5 million in profits without being subject to additional taxation. But the Com/Energy group—a unitary business, of which Canal is a part—earned less than $1 million of its $21 million business profits in New Hampshire, with the rest attributable to other States.[10] As a result, Com/Energy and Canal are fully subject to tax both on their owner-

profits, a Seabrook owner is able to earn $12.50 in New Hampshire business profits tax-free for each dollar of Seabrook Tax.

[9] Given that the New Hampshire apportionment formula includes ownership of property in New Hampshire as one factor, and given that each Seabrook owner by definition owns property (i.e. Seabrook) in New Hampshire, it follows that any profitable Seabrook owner will have some New Hampshire profits. It is the location of other property, as well as the location of personnel and sales, that determines where the remaining business profits are earned.

[10] Ch. 83-D:6 provides that "[i]f the person liable for the [Seabrook Tax] is a member of a unitary business within the meaning of RSA 77-A:1, XIV, then the entire amount of the tax due under this chapter shall be allowed as a credit pursuant to RSA 77-A:5, VI, against the tax liability of such unitary business under RSA 77-A." In the case of a unitary business, therefore, the credit will reduce liability for tax on the business profits of the unitary business as a whole—but, again, only to the extent that those profits are earned in New Hampshire.

ship of Seabrook and, except to a small degree, on their earning of business profits as well.

Some owners of Seabrook have more extensive operations in New Hampshire and, in consequence, a greater amount of New Hampshire business profits. New England Power is part of a unitary business that includes Granite State Electric Company—a New Hampshire utility—and it has both employees and sales in New Hampshire. Paying almost $2.4 million in Seabrook Tax in 1992, it is able to earn nearly $30 million in tax-free business profits, so long as those profits are earned in New Hampshire. Although it falls short of that figure, it is expected to be free of tax liability on $20 million in profits, leaving only $10 million of potentially sheltered income subject to taxation. The situation is similar for Northeast Utilities, which acquired Public Service Company of New Hampshire ("PSNH") in 1992. Using projections for 1993—the first full year following the acquisition—Northeast Utilities, through its subsidiaries North Atlantic Energy Co. and Connecticut Light and Power,[11] will pay an estimated $9.5 million in Seabrook Tax and thus might earn up to $118 million in business profits without further liability. Northeast Utilities will be quite close: its New Hampshire earnings for 1993 are projected to be $104.5 million.

The use of the offset afforded by the Seabrook Tax—like the Seabrook Tax itself—ultimately affects the wholesale and retail rates charged by Seabrook owners. For owners doing business primarily outside of New Hampshire, the credit will do little to reduce the taxes on their overall business profits, and those higher taxes will be passed through to their customers. For example, United

[11] Both Connecticut Light and Power and the North Atlantic Energy Corp. are subsidiaries of Northeast Utilities. Stip. ¶¶ 1.6, 3.7. North Atlantic owns the share of Seabrook previously owned by PSNH, which is now a subsidiary of Northeast Utilities as well. Stip ¶¶ 3.6-3.7.

Illuminating Company pays slightly less than one-half of the amount of Seabrook Tax paid by the Northeast Utilities companies ($4.2 compared to $9.5 million), but, as a result of the fact that its profits are earned primarily in Connecticut, it can shelter from taxation only a small fraction (less than 4%) of the business profits that Northeast Utilities can shelter ($3.6 million compared to $104.5 million). As taxes are then paid to other States on those profits earned outside of New Hampshire, the taxes will be reflected in rates charged to customers of United Illuminating. The same effects will be felt by customers of other Seabrook owners, to a greater or lesser degree depending upon the extent of the owners' business profits in New Hampshire.

3. *This Litigation.* The States of Connecticut, Massachusetts, and Rhode Island initiated this original action—pursuant to article II, § 2, cl. 1 and 2 of the United States Constitution and 28 U.S.C. § 1251(a)(1) (1991)—by filing a motion for leave to file a complaint in this Court. The complaint alleged, among other things, that the Seabrook Tax, taken together with the credit against liability for the New Hampshire Business Profits Tax, violated the Commerce Clause and 15 U.S.C. § 391. The State of New Hampshire opposed the motion for leave to file, asserting that "[t]he character of the injury alleged here . . . is merely economic" (Br. in Opp. at 8), that relief is available in other courts (Br. in Opp. at 9-10), that the claims would require an "[e]xtensive [t]rial" (Br. in Opp. at 10), that the claims were "premature" (Br. in Opp. at 12), and that the injury claimed by the States was "[n]ot [s]erious" (Br. in Opp. at 12). The Court granted the plaintiff States leave to file their complaint. 112 S. Ct. 962 (1992).

The Court subsequently referred the case to the Special Master. 112 S. Ct. 1756 (1992). Several weeks later, the Court also referred the motion by certain Seabrook owners to intervene—which had been filed shortly before the initial referral to the Special Master—to the Special Master for decision. 112 S. Ct. 1930 (1992). The Special Master then recommended that the motion be granted, noting that "[t]o the extent the regulatory authorities do not allow the Utilities to pass the tax along to consumers through increased rates, the Utilities suffer an immediate injury that the Plaintiff States do not represent." First Interim Report at 8. The Special Master further observed that "[e]ven if the regulatory authorities permit the Utilities to pass the entire tax through to consumers, they still suffer a distinct injury in that increased rates are likely to dampen demand and to raise regulatory resistance to other, independently justified rate increases." First Interim Report at 8.[12] The Court adopted the recommendation of the Special Master and granted the Utilities' motion to intervene. 112 S. Ct. 2961-62 (1992).

Working under the direction of the Special Master, the parties developed a stipulated record in the case. That record was submitted to the Special Master at the Fourth Meeting of Counsel on September 9, 1992. Based upon that record, and the subsequent briefs and argument presented by the parties, the Special Master concluded (and recommended that this Court conclude) that the New Hampshire tax scheme violated both the Commerce Clause and 15 U.S.C. § 391.

The Special Master began with the statutory challenge, determining that New Hampshire had (in the words of the statute) "impose[d] . . . a tax on or with respect to the generation or transmission of electricity which discriminates against out-of-state manufacturers, producers, wholesalers, retailers, or consumers of that electricity." 15 U.S.C. § 391. The Special Master first rejected the argument that the Seabrook Tax—"a tax exclusively on property that by definition is used in generating, produc-

[12] The Special Master also concluded that "considerations of judicial economy . . . weigh in favor of intervention by the Utilities." First Interim Report at 9.

ing, supplying and distributing electric power" (Final Report 19)—is somehow not "a tax on or with respect to the generation or transmission of electricity" (15 U.S.C. § 391), finding that narrow construction to be inconsistent with the more inclusive language of Section 391. Final Report 18-19. Then, relying on the decision in *Arizona Pub. Serv. Co. v. Snead,* 441 U.S. 141 (1979) (striking down a New Mexico tax scheme as discriminatory under Section 391), the Special Master concluded that the New Hampshire scheme "replicates the flaw identified by this Court in the New Mexico Electrical Energy Tax scheme: allowance of a credit for a local tax paid against a separate local tax owed, with a resultant discrimination against interstate commerce." Final Report 20.

The Court found the New Hampshire tax scheme to be discriminatory under the Commerce Clause as well. Although New Hampshire had argued that it had done nothing more than enact a neutral *ad valorem* property tax, the Special Master found that description of the tax scheme to be incomplete: "[t]he fact that the Seabrook Tax and the credit provision were enacted in the same legislative act suggests that they were intended to function together to impose a new property tax levy and simultaneously to provide relief in the same amount from the Business Profits Tax on income allocable to New Hampshire business activity." Final Report 27. The Special Master pointed out that, like similar tax schemes invalidated by this Court, the New Hampshire scheme "affirmatively places interstate commerce at a disadvantage by giving preferential tax treatment to companies with more significant intrastate activities." Final Report 28-29; *see, e.g., Maryland v. Louisiana,* 451 U.S. 725 (1981); *Westinghouse Elec. Corp. v. Tully,* 466 U.S. 388 (1984). The scheme thus was directly contrary to "the principle that a State may not use its power to tax in a manner that places interstate commerce at a disadvantage in competition with intrastate commerce." Final Report 35.

The Special Master noted that "[t]he unconstitutionality of the New Hampshire Seabrook Tax and credit scheme is confirmed by application of the 'internal consistency' test." Final Report 36. If every State were to adopt the tax scheme employed by New Hampshire—the working hypothesis upon which the "internal consistency" test is based—"then utilities owning 'nuclear property' in one State but earning part of their income elsewhere would face a risk of multiple taxation not faced by utility owners conducting all of their business activity within a single State." Final Report 37. Because the New Hampshire scheme uses a tax credit to offset liability for one local tax against liability for a second local tax, it "favors those Seabrook owners earning profits on business activity in New Hampshire over those owners earning equivalent business profits partly in other States." Final Report 37. That favoritism, as the Special Master observed, "is contrary to the basic Commerce Clause principle that 'a State may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.' " Final Report 37-38 (quoting *Armco, Inc. v. Hardesty,* 467 U.S. 638, 642 (1984)).

Turning to the remedy, the Special Master recommended that this Court provide retroactive relief in the form of a refund of taxes paid less any credit taken against New Hampshire business profits taxes. The Special Master found no basis for making the rulings in this case prospective only, saying both that the recommended decision "results from a straightforward application of existing law to the present facts" (Final Report 40) and that "it reasonably should have been apparent to New Hampshire that its Seabrook Tax and credit scheme was of dubious constitutionality" (Final Report 41). The Court further found the Eleventh Amendment to be no bar to relief, stating that the plaintiff States, as in *Maryland v. Louisiana,* 451 U.S. 725 (1981), were suing "to recover for injuries to themselves, as well as to the great majority of their citizens," and not for relief "on behalf of specific individuals." Final Report 41. And the Special Master decided that a refund was the proper remedy becauses New Hampshire, by declaring that the Seabrook Tax and credit were nonseverable, had made clear that the provisions were to be "considered a unit." Final Report 43. Given that the tax could not exist without the credit, and given that the tax and credit could not constitutionally exist together, the proper course is to "recogniz[e] that the Seabrook Tax and credit were unconstitutional from the start" and "put the parties back into the positions they would have held if New Hampshire had never adopted its unconstitutional tax scheme." Final Report 44.

SUMMARY OF ARGUMENT

The Special Master correctly concluded that the New Hampshire tax scheme discriminates against interstate commerce in violation of the Commerce Clause and Section 391. Although the Seabrook Tax itself purports to treat all businesses equally, the linkage of that tax, by means of a dollar-for-dollar credit, to payment of a second New Hampshire tax (the Business Profits Tax) creates a clear favoritism for those Seabrook owners doing substantial business in New Hampshire over those Seabrook owners doing equivalent business in other States. This Court has repeatedly struck down, under both the Commerce Clause and Section 391, efforts by States to use discriminatory tax credits and exemptions in order to protect businesses conducting in-state activities from multiple taxation, while leaving businesses conducting interstate activities exposed to that risk. *See Tyler Pipe Indus., Inc. v. Washington Dep't of Revenue*, 483 U.S. 232 (1987) (Commerce Clause); *American Trucking Ass'ns, Inc. v. Scheiner,* 483 U.S. 266 (1987) (Commerce Clause); *Armco, Inc. v. Hardesty,* 467 U.S. 638 (1984) (Commerce Clause); *Westinghouse Elec. Corp. v. Tully,* 466 U.S. 388 (1984) (Commerce Clause); *Maryland v. Louisiana,* 451 U.S. 725 (1981) (Commerce Clause); *Arizona Pub. Serv. Co. v. Snead,* 441 U.S. 141 (1979) (15 U.S.C. § 391). The principles of those cases—whether employing constitutional or statutory analysis, and whether utilizing the "internal consistency" test or not—make clear that the New Hampshire tax scheme cannot stand.

The Special Master was also correct in determining that a refund of taxes paid (minus any amounts taken as a credit) was the proper form of retroactive relief. There is no basis for making the constitutional or statutory rulings prospective only, and the Eleventh Amendment is no barrier to an award of retroactive relief to the plaintiff States, even though the owners of Seabrook are the intermediaries by which it is obtained. And it is too late in the day for New Hampshire to claim what the statute on its face expressly *dis*claims: that, absent the credit, the legislature in 1991 would simply have enacted the Seabrook Tax anyway. It is thus entirely appropriate, by way of remedy, to restore the plaintiffs to the position that they would have occupied "if New Hampshire had never adopted its unconstitutional tax scheme." Final Report 44.

ARGUMENT

I. THE SEABROOK TAX AND CREDIT PROVISION, TAKEN TOGETHER, DISCRIMINATE IN FAVOR OF LOCAL COMMERCE IN VIOLATION OF THE COMMERCE CLAUSE AND FEDERAL LAW (15 U.S.C. § 391)

A. The Seabrook Tax and Credit Provision, Taken Together, Violate the Commerce Clause

Although the Commerce Clause is on its face a grant of power to Congress, this Court has long accepted the proposition that the Clause " 'by its own force created an area of trade free from interference by the States.' " *American Trucking Ass'ns, Inc. v. Scheiner,* 483 U.S. at 280 (quoting *Boston Stock Exchange v. State Tax Comm'n,* 429 U.S. 318, 328 (1977)); *see Wyoming v. Oklahoma,* 112 S. Ct. 789, 800 (1992).[13] Thus, while States may properly require businesses engaged in interstate commerce to pay their own way, they may do so only by taxes that, among other things, "do[] not discriminate against interstate commerce." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). "One primary consequence of this constitutional restriction on state taxing powers . . . is that 'a State may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.' " *American Trucking Ass'ns, Inc. v. Scheiner,* 483 U.S. at 280 (quoting *Armco, Inc. v. Hardesty,* 467 U.S. at 642).

State taxation may discriminate on its face or in actual operation. Here, we submit, the New Hampshire tax scheme does both. Applying the test employed by the

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[13] As we did before the Special Master, we discuss the constitutional issue before the statutory issue because the principles with regard to discrimination against interstate commerce have been more fully developed in that context. The Special Master ultimately found that the New Hampshire scheme was invalid on both constitutional and statutory grounds, though he addressed the statutory argument first.

Court with respect to claims of facial discrimination—the "internal consistency" test—it is readily apparent that the Seabrook Tax and the accompanying credit against liability for the New Hampshire Business Profits Tax are not internally consistent: that is, according to their own taxing principles, they expose interstate commerce to burdens not faced by wholly local operations. But, even without regard to the "internal consistency" test, it is clear that the tax system works just as it was designed to work: businesses with a greater amount of New Hampshire profits are favored over businesses with equal profits in other States. The statute thus "unquestionably discriminates against interstate commerce in favor of local interests." *Maryland v. Louisiana,* 451 U.S. at 756.

1. *The New Hampshire Tax Scheme Is Not Internally Consistent.* The Court first expressly applied the "internal consistency" test as a means of determining whether state taxes on multistate businesses were fairly apportioned to reach only that business conducted within the State. *See Container Corp. of America v. Franchise Tax Bd.,* 463 U.S. 159, 169 (1983); *Goldberg v. Sweet,* 488 U.S. 252 (1989). The Court later held, however, that "[a] similar rule applies where the allegation is that a tax on its face discriminates against interstate commerce." *Armco, Inc. v. Hardesty,* 467 U.S. at 644. *See also Tyler Pipe Indus., Inc. v. Washington Dep't of Revenue,* 483 U.S. at 240-48 (implicitly applying test); *American Trucking Ass'ns, Inc. v. Scheiner,* 483 U.S. at 284-87 (explicitly applying test).[14]

[14] In its brief, New Hampshire spends page after page trying to establish that this unequivocal statement does not mean what it says. *See* N.H. Br. at 27-35. Referring to (but not naming) "numerous opinions of this Court indicating that the test should not be applied in a case of this type," N.H. Br. at 28, the State goes on to establish nothing more than that the test has been most frequently used to determine whether taxes are fairly apportioned. But its use in that context does not nullify its use in cases of discrimination as well; the Court in *Armco,* while employing the test with respect to

Applying the test to claims of facial discrimination, the Court has said that, to "have 'what might be called internal consistency . . . the [tax] must be such that, if applied by every jurisdiction,' there would be no impermissible interference with free trade." *Armco, Inc. v. Hardesty*, 467 U.S. at 644 (quoting *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. at 169). The test, therefore, does not look to whether a multistate business in fact pays more tax than a wholly intrastate business; rather it looks to whether the state tax scheme, by its own principles, creates the risk of such unequal burdens.[15] In *Armco*, where the State exempted local manufacturers from paying the state wholesale tax, and in *Tyler Pipe*, where the State exempted local wholesalers from paying the state manufacturing tax, the Court had no difficulty in concluding that discrimination was present: if every State had either tax system—the assumption made for purposes of applying the "internal consist-

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a claim of discrimination, expressly noted its origins in cases involving fair apportionment. 467 U.S. at 644. Indeed, New Hampshire ultimately appears to concede that the test *is* used in discrimination cases but then says that its use in that context is only to "evaluate compensating tax defenses." N.H. Br. at 30. This argument makes no sense at all. Even a cursory reading of *Armco, Inc.* and *Tyler Pipe* shows unmistakably that the inquiry into "internal consistency" and the inquiry into "compensating taxes" are two separate inquiries, although, of course, they may occur in the same case. The purpose of an inquiry with respect to "compensatory taxes" is not to identify whether discrimination has occured but simply to determine whether activities are so related that a tax on one activity can fairly be said to compensate for the inability to tax a second activity. The "internal consistency" test is not designed, and has not been used, to answer that latter question.

[15] Explaining that actual multiple taxation need not be shown, the Court in *Armco, Inc. v. Hardesty* stated: "[a]ny other rule would mean that the constitutionality of [a State's] tax laws would depend on the shifting complexities of the tax codes of 49 other States, and that the validity of the taxes imposed on each taxpayer would depend on the particular other States in which it operated." 467 U.S. at 644-45.

ency" test—then companies doing their manufacturing and wholesaling in a single State would pay only one tax on those activities, while companies conducting the activities in two or more States would be subject to multiple taxation. 467 U.S. at 644-45; 483 U.S. at 246-48. The result is intrinsic discrimination against interstate conduct of those multiple commercial activities in favor of wholly intrastate conduct of the same activities.

The New Hampshire tax scheme suffers from precisely the same flaw. As structured, the statute assures a Seabrook owner that it will be immune from tax on its business profits, up to the amount of the Seabrook Tax, so long as those business profits are earned in New Hampshire; if some or all of those business profits are earned in other States, however, then the owner is faced with paying both the Seabrook Tax and taxes in the other States on the unsheltered business profits. Thus, for example, if two Seabrook owners each paid $1 million in Seabrook Tax, and one owner conducted all its business in New Hampshire and the other conducted all its business (except for ownership of Seabrook) in Connecticut, the first owner would face no tax liability at all on the first $12.5 million of its business profits, while the second owner would be subject to taxation on virtually all of the first $12.5 million of its business profits (except for the small amount attributed to New Hampshire as a result of owning Seabrook). That difference—resulting solely from the interstate or intrastate nature of the business—is discrimination, plain and simple.[16]

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[16] New Hampshire proposes an odd codicil to the "internal consistency" test under which the Court would assume not only that each State adopted the New Hampshire tax scheme but that the hypothetical taxpayers conducted all activities subject to taxation in each State. All this would do, of course, is muddle the comparison between intrastate and interstate business—perhaps the point of the suggestion—by attributing some "intrastate" activity to the interstate business and some "interstate" activity to the intrastate business. In a test that compares the effects of a taxing principle on

The "inconsistency" in this scheme results from the fact that New Hampshire has not applied a neutral principle to determine whether the activities of owning Seabrook and of earning business profits—like the activities of manufacturing and wholesaling at issue in *Armco* and *Tyler Pipe*—are activities properly subject to multiple taxation, or whether they are not. For example, a tax system that gave no credit for payment of the Seabrook Tax would be consistently treating the activities as separate and therefore subject to multiple taxation; or a tax system that (to take one possibility) reduced the Seabrook Tax by tax paid on business profits to *any* State would be consistently treating the activities as integrated and therefore subject only to a single tax. Each such tax scheme would be internally consistent: no company would be worse off for conducting the activities in different States rather than in one State. What is inconsistent, and hence impermissible, however, is the approach taken by the New Hampshire legislature—to treat the activities as properly subject to multiple taxation if performed in different States, but only to single taxation if performed in New Hampshire. *See American Trucking Ass'ns, Inc. v. Scheiner,* 483 U.S. at 306 (Scalia, J., dissenting) ("[a] credit against intrastate taxes falls readily within the highly suspect category").[17]

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interstate businesses and on intrastate businesses, it hardly seems sensible to make the categories less distinct. Moreover, to the extent that this new set of assumptions might decrease the amount of discrimination in any particular case, it would do so for exactly the reason that one would think: the discrimination is more beneficial to businesses as their intrastate activity increases and less beneficial as it decreases.

[17] As we have discussed in our "Exceptions and Brief in Support for Intervenors," filed on March 15, 1993, the Seabrook Tax is discriminatory even without regard to the provision for credit against the Business Profits Tax. The reason, however, is that New Hampshire has deliberately placed a special burden on one facility used primarily in interstate commerce, not that the Seabrook Tax, taken by itself, is internally inconsistent.

Although New Hampshire says that, in allowing the credit, the State is merely deciding "not to tax a portion of the business profits that it is clearly entitled to tax," N.H. Br. at 34-35, that statement, while true, is wholly beside the point. Far from offering a justification for its discrimination, New Hampshire is simply restating what credits do: every discriminatory credit could be described in such terms. Thus, West Virginia in *Armco* could say that it was not imposing a tax on certain sales (those subject to the local manufacturing tax), or Washington in *Tyler Pipe* could say that it was not imposing a tax on certain manufactured items (those subject to the local wholesale tax). Regardless of the description, however, the fact remains that the two activities are treated as subject to a single tax, and the decision "not to tax" is made, *only* if they both are performed in-state. It is just that sort of parochial favoritism that the Commerce Clause serves to forbid.

We recognize, of course, that interstate commerce often may wind up bearing a greater tax burden than purely intrastate commerce, but that fact does not, as New Hampshire appears to believe (N.H. Br. at 42), mean that the existence of a heavier burden is a matter of indifference under the Commerce Clause. A principal benefit of applying the "internal consistency" test in discrimination cases is that it distinguishes, on the one hand, cases in which the risk of multiple taxation of interstate activities arises from application of different tax principles by different States (permissible under the Commerce Clause) from, on the other hand, cases in which the risk of multiple taxation arises from application of discriminatory tax principles by a particular State (impermissible under the Commerce Clause). For example, if Washington has a tax on manufacturing (but no tax on wholesaling) and Oregon has a tax on wholesaling (but no tax on manufacturing), a company doing interstate business may pay two taxes—by manufacturing in Washington and wholesaling in Oregon—as a result of the different tax choices made by the two States. But each tax is itself internally consistent because, if every State taxed only manufacturing (like Washington) or only wholesaling (like Oregon), both interstate and intrastate business would be on exactly the same footing (paying one tax).[18] If Washington taxes both wholesaling and manufacturing, however, and further credits the state wholesale tax against the state manufacturing tax, the internal consistency is lost: then a Washington manufacturer wholesaling in Washington pays just once, while a Washington manufacturer wholesaling in Oregon pays twice. This inequality—and the fact that it arises from a single, discriminatory tax principle—are immediately apparent upon application of the "internal consistency" test.

The inability of the New Hampshire tax scheme to satisfy the "internal consistency" test is enough, in and of itself, to establish its unconstitutionality. *See Armco, Inc. v. Hardesty*, 467 U.S. at 644-46 (striking down tax scheme based on discriminatory structure); *Tyler Pipe Indus., Inc. v. Washington Dep't of Revenue*, 483 U.S. at 240-48 (same). As we discuss in the next section, however, it is also clear that the scheme can and does produce the discriminatory effects dictated by its discriminatory structure.

2. *The New Hampshire Tax Scheme Necessarily Discriminates in Actual Operation.* a. Even prior to explicit application of the "internal consistency" test, this Court had struck down systems of taxes and tax credits that, taken together, conferred a preference on local business. In *Maryland v. Louisiana*, for example, the Court found that a Louisiana tax scheme "unquestionably discriminates against interstate commerce in favor of local interests as

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[18] In addition, the nature of the respective tax schemes means that in some cases—those involving Oregon manufacturers selling at wholesale in Washington—interstate commerce would fare *better* than wholely intrastate commerce, paying no tax as opposed to a single tax.

the necessary result of various tax credits and exclusions." 451 U.S. at 756. The Court observed that Louisiana had exempted natural gas "used for certain purposes within Louisiana" from its First-Use tax, while "[c]ompetitive users in other States are burdened with the Tax." 451 U.S. at 756. Moreover, as part of the same tax scheme, Louisiana had "provide[d] important tax credits favoring local interests." *Id.*[19] Although the Court recognized that "further hearings would be required to provide a precise determination of the extent of the discrimination in this case," 451 U.S. at 759-60, it nevertheless struck down the Louisiana tax system, stating that it "need not know how unequal the Tax is before concluding that it unconstitutionally discriminates." 451 U.S. at 760.

The Court reached a similar conclusion in *Westinghouse Elec. Corp. v. Tully*. There, it struck down as discriminatory a New York tax scheme that provided an escalating credit against New York income tax as businesses conducted more of their shipping activities within the State. The Court noted that the credit provision discriminated against businesses operating outside of New York because it "ha[d] the effect of allowing a parent a greater tax credit on its accumulated DISC income as its subsidiary DISC moves a greater percentage of its shipping activities into the State of New York. Conversely, the adjustment decreases the tax credit . . . as the DISC increases its shipping activities in other States." 466 U.S. at 400. The tax scheme, therefore, not only "provide[d] a positive incentive for increased business activity in New York State," but also "penalize[d] increases in . . . shipping activities in other States." 466 U.S. at 400-01 (internal citation omitted). *See also Boston Stock Ex-*

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[19] Of particular relevance here, Louisiana provided that payors of the First-Use Tax to Louisiana could credit that payment against liability for severance taxes in Louisiana. 451 U.S. at 756. The credit was of value, therefore, only to the extent that taxpayers conducted a second taxable activity in the State.

change v. State Tax Comm'n, supra (striking down tax credit as discriminatory).

These cases—and later cases like *Armco* and *Tyler Pipe,* discussed earlier—make absolutely clear that States cannot use an interlocking scheme of taxes and tax credits to favor local commerce, any more than they can do so by a single discriminatory tax. Yet, in tying together the Seabrook Tax and a compensating credit against tax on local business profits, that is precisely what New Hampshire has done. In effect, the tax and credit provisions have created a sliding scale pursuant to which companies can offset tax on their business profits to the extent that they earn their profits in New Hampshire and not elsewhere. Until the credit is exhausted, the system directly rewards companies as their business profits increase within the State and directly penalizes companies whose profits arise in other States.[20]

Although many of the relevant cases involved taxes on discrete transactions, instead of aggregate taxes (like income taxes), that fact does not change the constitutional analysis. On the contrary, the Court has expressly refused to draw any such distinction. *See Westinghouse*

[20] Although New Hampshire tries to distinguish *Maryland v. Louisiana*—arguing that credit for payment of the First-Use Tax against state severance taxes was discriminatory because it "was only available if the taxpayer was engaged in the business of extracting natural resources within Louisiana" (N.H. Br. at 46)—its discussion actually confirms that the New Hampshire statute, just like the Louisiana statute, is discriminatory. Just as the First-Use taxpayer in Louisiana could claim a credit only against taxes upon extraction in Louisiana (and not in other States), a Seabrook taxpayer in New Hampshire can claim a credit only against taxes on income earned in New Hampshire (and not in other States). Put another way, the credit for payment of tax on one in-state activity (here, ownership of Seabrook) is "only available" if, and to the extent that, a taxpayer conducts a second activity subject to tax in the same State. The discrimination here is thus no different from—indeed, takes the very same form as—the discrimination found in *Maryland v. Louisiana.*

Elec. Corp. v. Tully, 466 U.S. at 404. There, the Court rejected an argument that the principles banning discrimination with respect to "transactional taxes" are inapplicable to "taxes on general income," observing: "It cannot be that a State can circumvent the prohibition of the Commerce Clause against placing burdensome taxes on out-of-state transactions by burdening those transactions with a tax that is levied in the aggregate—as is the franchise tax—rather than on individual transactions." *Id.* It is thus the fact of the discrimination, not the form of the discrimination, that is controlling.[21]

The *extent* of discrimination suffered by each Seabrook owner depends, of course, upon the extent of its business in New Hampshire. For companies like United Illuminating and Canal, which (apart from ownership of Seabrook) do no business in New Hampshire, the capacity to exempt their business profits from taxation is limited at best. Thus, United Illuminating (paying $4.2 million in Seabrook Tax) escapes tax on just $3.6 million of its business profits; Canal (paying $850,000 in Seabrook Tax) and its related companies escape tax on less than $1 million of their business profits. Yet, if those companies did more of their business in New Hampshire, they could earn up to $52.5 million and $10.5 million in business profits, respectively, without facing additional tax

[21] New Hampshire correctly notes (N.H. Br. at 48) that the Court in *Westinghouse Elec. Corp. v. Tully* said that "it is not the provision of the credit that offends the Commerce Clause, but the fact that it is allowed on an impermissible basis . . . ." 466 U.S. at 406 n.12. But there is nothing helpful to New Hampshire in that observation, which makes the straightforward point that credits do not violate the Commerce Clause in and of themselves, but only when they operate on a discriminatory basis. The Special Master, of course, did not say that all credits are impermissible; rather, he concluded that the operation of the credit here—like the credits and exemptions in *Westinghouse, Maryland v. Louisiana, Armco, Inc.* and other cases—did discriminate against interstate commerce.

liability. Because their business is conducted in other States, however, the equivalent level of business profits is fully subject to tax.[22]

Companies like New England Power and Northeast Utilities, by contrast, are freed of the obligation to pay tax on a far more significant amount of their business profits. Because each of them has substantial operations in New Hampshire, they are relieved of liability for tax on profits of $20 million (NEP, 1992) and $105 million (NU, 1993), based on payments of Seabrook Tax of $2.4 million and $9.5 million, respectively. It should be noted, however, that even these companies suffer *some* present, identifiable discrimination: because each of them is expected to have some unused credit, they would be able to offset tax on even more business profits if those profits were earned in New Hampshire rather than in other States. And all companies must take the discriminatory tax scheme into account in making business decisions about whether to locate new (or even existing) property, personnel, and sales in or out of New Hampshire. *See American Trucking Ass'ns, Inc. v. Scheiner*, 483 U.S. at 283 (relevant to ask "if the revenue measures maintain state boundaries as a neutral factor in economic decisionmaking").

b. New Hampshire nonetheless claims that it shows "no favoritism toward owners engaged in intrastate sales of electricity." N.H. Br. at 27. To the extent that this argument rests upon the coincidence that PSNH suffered losses in 1991 and 1992, it is simply off-the-mark: as the Special Master pointed out, the important point is that "the Seabrook Tax credit 'backstopped' any intrastate utility, *guaranteeing* that, no matter what its profits

[22] Although we do not think it necessary to prove actual multiple taxation, the fact is that each of the owners of Seabrook Station (except for governmental entities) is subject to taxation on business profits in other States in which it does business. *See* Final Report 11-12; Stip. ¶ 2.4.

picture or its tax status, its intrastate customers would pay only one tax up to the point of the full Seabrook Tax paid." Final Report 22. By its very structure, the system of interlocking taxes and credits assures an owner that it will be fully protected from tax on its profits, up to the amount of the credit, so long as it earns those profits within the State, an assurance not given to owners earning equivalent profits in other States. That discrimination is always present, even where—because of fortuitous circumstances like lack of profitability—it does not have full effect on each of the Seabrook owners in a given year. Unless *all* Seabrook owners are and always remain unprofitable (and, thus, have no potential liability for tax on profits in *any* State) or unless *all* Seabrook owners always use up the entire amount of their credit [23] —neither of which circumstances is even remotely likely —the statute will inevitably create differences among Seabrook owners based solely upon whether their profits are earned in New Hampshire or other States. That continuing, pervasive discrimination is barred by the Commerce Clause.

In any event, it is flatly incorrect to claim that those companies with greater in-state sales are not favored by the statute.[24] The figures just discussed make clear that

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[23] Even if all Seabrook owners used up all of their respective credits, the statute would be exerting the same "hydraulic pressure" to earn income in New Hampshire and not in other States. Thus, whether or not the particular differences among Seabrook owners were eliminated in that situation (not, in any event, present here), the statute would still be producing effects prohibited by the Commerce Clause. *See* note 28 *infra*.

[24] The discriminatory effects of the New Hampshire tax scheme are fully apparent from the facts demonstrating operation of the scheme from its enactment to the present. We note in passing, however, that use of projections to illustrate the likely effects in future years is a perfectly reasonable means of assessing the legitimacy of the tax scheme. Even though New Hampshire complains about any reliance on projections, the State has itself relied on projections—indeed, projections made by Northeast Utilities, one

New England Power, paying $1.8 million *less* in Seabrook Tax than United Illuminating, is able to earn almost $17 million *more* in business profits without incurring any additional tax liability. That result comes about for one reason and one reason only: those profits are earned in New Hampshire, rather than in another State. The projected figures for Northeast Utilities show the same sort of favoritism in, if anything, even more striking terms. *See* page 25 *supra.*[25]

It is also misguided for the State to claim that "the failure to tax business profits since the Nuclear Property Tax was enacted has been more meaningful for interstate than for in-state utilities." N.H. Br. at 52. Even if that were correct (*but see* pages 24-25 *supra*), an inquiry into whether various Seabrook owners make greater or lesser use of the credit against liability for the New Hampshire Business Profits Tax is not the proper inquiry because it looks at only one side of the equation: taxes in New Hampshire. To identify discrimination, it is necessary to ask, not just whether the credit allows owners of Seabrook to escape liability for income taxes *in New Hampshire,* but whether owners earning profits largely in other States are faced with liability not faced by businesses earning equivalent profits in-state; *that* question requires consideration, not just of their exposure to income taxes

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of the Seabrook owners—to resolve important matters with respect to utility reorganization. *See In re Northeast Utilities/Public Service Company of New Hampshire Reorganization Proceedings,* 114 P.U.R.4th 385, 400 (1990) (State sought finding that "NU has met its burden of proving that its underlying assumptions regarding the Rate Agreement and its financial forecasts are reasonable . . .").

[25] As the Special Master pointed out, Final Report 29-33, the reason that Northeast Utilities receives these significant benefits from the New Hampshire tax scheme—as compared to United Illuminating, for example—is that it acquired PSNH in 1992, thus greatly increasing the amount of business that Northeast Utilities conducts in New Hampshire.

in New Hampshire, but of their exposure in other States as well.[26]

The correct nature of the inquiry is again made clear by the prior cases striking down discriminatory tax schemes. For example, in *Maryland v. Louisiana*, it was self-evident that a business paying the First-Use Tax to Louisiana but not extracting any minerals there was no worse off *in Louisiana* than another company paying the First-Use Tax and using the credit against liability for Louisiana severance taxes: in that situation, *neither* company would face liability in Louisiana for severance taxes (up to the amount of First-Use Tax paid). But the critical element is that the interstate business *does* face liability for severance taxes elsewhere, for which its credit does it no good. When that potential liability is taken into account—as it must be to identify discrimination between intrastate and interstate commerce—then it is immediately apparent that the credit provision offsetting one local tax against another does have a discriminatory effect: it "encourage[s] natural gas owners involved in the production of OCS gas [and thus paying the First-Use Tax to Louisiana] to invest in mineral exploration and development within Louisiana rather than to invest in further OCS development or in production in other States." 451 U.S. at 757.

The inequality in the New Hampshire tax scheme can be readily seen, in fact, by looking at the two taxes in

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[26] This point plainly escapes New Hampshire. In its discussion of the effects of its tax scheme, it repeatedly addresses only the exposure of Seabrook owners to taxes in New Hampshire and makes no effort to discuss exposure to taxes in other States on equivalent activities (except to make the obvious, and irrelevant, point that all States apportion income). *See, e.g.*, N.H. Br. at 47, 52-53. As a result, it does not make any meaningful comparisons between companies similarly situated except for the States in which they earn their profits—the necessary comparison for a claim of discrimination of this sort.

reverse order. If New Hampshire had written its statute to provide that "any business profits tax paid to New Hampshire (but not to any other State) shall be credited against liability for the Seabrook Tax," the discrimination against companies earning their profits in other States would have been obvious, just as was the discrimination in *Armco* against companies paying manufacturing taxes elsewhere but not allowed to deduct them against the West Virginia wholesale tax. But a tax scheme is no less discriminatory merely because the taxes and credit provision are turned around. *See Tyler Pipe, supra* (striking down a statute reversing the credit at issue in *Armco*). Here, for the Seabrook owners, the effect of the present tax scheme is identical to the effect of the hypothetical statute set out above: in either case, companies with New Hampshire profits are able to avoid multiple taxation to the extent of, but only to the extent of, those profits.

It is theoretically possible, of course, for Seabrook owners to lessen, or even avoid, the discrimination inherent in the New Hampshire tax scheme by increasing the amount of business that they do in New Hampshire. But that is hardly a defense of the scheme. In the first place, it will often be very costly—and in the context of utility companies subject to regulatory oversight, simply not practical or realistic—for a business to shift a substantial amount of its operations into a particular State. The owners of Seabrook, for the most part, make wholesale sales to affiliated companies and retail sales in franchised areas outside of New Hampshire. It would require a general restructuring of their businesses—or the acquisition, perhaps, of New Hampshire utilities (see note 25 *supra*)—to provide them significant relief from the inequality of the tax system. Imposition of such a burden only on companies not already conducting their affairs in-state is itself discriminatory. *See Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. at 336 (condemning use of "power to tax an in-state operation as a means of requiring [other] business operations to be performed in the home State") (internal quotes omitted).

In any event, the argument is legally insufficient. Only last Term, the Court declined to accept a similar argument, finding "no authority" for the notion "that a tax that does discriminate against foreign commerce may be upheld if a taxpayer could avoid that discrimination by changing the domicile of the corporations through which it conducts its business." *See Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue and Finance*, 112 S. Ct. 2365, 2370 (1992).[27] Indeed, any other conclusion would be intolerable since, in virtually any case of discrimination, the disadvantaged taxpayer retains the "option" either to succumb to the discrimination or to seek entry into the favored class. Thus, in *Westinghouse Electric Corp. v. Tully*, the taxpayer could have shifted shipping operations to New York; in *Armco* the taxpayer could have chosen to manufacture goods in West Virginia; in *Tyler Pipe* a Washington manufacturer could have sold its products only within the State. Yet, despite these possible (if impractical) courses of action, the Court found each of the tax systems unconstitutional, making clear that States cannot make discriminatory tax schemes into a tool for penalizing companies that elect to do business outside their borders.[28]

[27] Although *Kraft* involved the Foreign Commerce Clause, the cases cited by the Court—*Westinghouse Electric Corp. v. Tully, supra*, and *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963)—make clear that its views are fully applicable to the domestic Commerce Clause as well.

[28] The Court, in fact, has invalidated state tax systems even where some out-of-state companies actually were able to take advantage of the discriminatory structure. Thus, in *American Trucking Ass'ns, Inc. v. Scheiner*, the Court struck down an unapportioned flat tax imposed on travel within Pennsylvania—on the ground that, viewed in terms of cost-per-mile, it generally favored intrastate truckers—even though it recognized that some interstate truckers traveled more miles in the State than some intrastate truckers. The Court found the skewing of business decisions itself to be inappropriate, stating that the tax had a "forbidden impact

Finally, although it is not necessary in order to establish a claim of discrimination, it should be noted that the inequality established by the New Hampshire statutes is anything but accidental. As the legislative history unmistakably shows, the New Hampshire legislature, faced (like many States) with a need for additional revenues, sought to define and impose a tax burden that would fall exclusively on out-of-state taxpayers. The credit provision was part of this strategy because it assured that PSNH, then the largest single owner of Seabrook, would be given substantial protection against taxation of future business profits. That the credit was of little benefit to most Seabrook owners, far from being a defect in the statute, was regarded as a positive feature. The Chairman of the legislative subcommittee that drafted the bill even described the taxing scheme as being "a tax in the New Hampshire tradition of finding some way for the other fellow to pay." Remarks of Rep. Robert Hayes, The N.H. House of Representatives Floor Debate Re: House Bill 64, April 2, 1991, pp. 25-26.

The statute operates just as intended. The less business a Seabrook owner has in New Hampshire, the greater is its exposure to multiple taxation. Like the tax scheme in *Tyler Pipe*, the New Hampshire tax scheme only "operates to impose a unified tax eliminating the risk of multiple taxation when the [activities] are both carried out within the State." 483 U.S. at 246. That it cannot do. "[A] state tax that favors in-state business over out-of-state business for no other reason than the location of its business is prohibited by the Commerce Clause."

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on interstate commerce because it exerts an inexorable hydraulic pressure on interstate businesses to ply their trade within the State that enacted the measure rather than 'among the several States.'" 483 U.S. at 286-87 (quoting U.S. Const., art. I, § 8. cl. 3). *See* Final Report 38 (noting that Seabrook Tax and credit scheme exert "hydraulic pressure" on Seabrook owners with unused credits to increase business activities in New Hampshire).

American Trucking Ass'ns, Inc. v. Scheiner, 483 U.S. at 286.[29]

B. The Seabrook Tax and Credit Provision, Taken Together, Violate Federal Law (15 U.S.C. § 391)

The Seabrook Tax and credit provision also violate the provisions of 15 U.S.C. § 391. That statute prohibits any State from "impos[ing] or assess[ing] a tax on or with respect to the generation or transmission of electricity which discriminates against out-of-State manufacturers, producers, wholesalers, retailers, or consumers of that electricity." Moreover, it broadly defines as discriminatory any tax that "results, either directly or indirectly, in a greater tax burden on electricity which is generated and transmitted in interstate commerce than on electricity which is generated and transmitted in intrastate commerce."

This Court, in *Arizona Pub. Serv. Co. v. Snead, supra,* relied upon Section 391 to strike down a New Mexico tax scheme that, like the New Hampshire system here, imposed a seemingly neutral tax on all companies engaged in a defined local activity, but then tied that tax, by means of a credit, to a second tax on a local activity. There, while all owners of the Four Corners power stations paid the first tax (an electrical energy tax) on equal terms, the credit allowed those companies selling in New Mexico to ameliorate its impact by reducing liability for the state gross receipts tax. The Court found the inter-

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[29] The State makes the traditional *in terrorem* argument: that, if its statute is struck down, States will be barred from using credits to encourage important activities. N.H. Br. at 50 n.24. But, in cases where credits are used for regulatory purposes (and not simply to favor local commerce), even discriminatory credits may be upheld so long as they are justified by "a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives." *New Energy Co. v. Limbach,* 486 U.S. 269, 278 (1988). Credits not meeting that standard, of course, are already subject to invalidation under *New Energy Co.*

play between the two taxes to be discriminatory, remarking: "The tax-credit provisions of the Act itself insure that locally consumed electricity is subject to *no* tax burden from the electrical energy tax, while the bulk of the electricity generated in New Mexico by the appellants is subject to a 2% tax, since it is sold outside the State." 441 U.S. at 149.

The legislative history of Section 391 shows that Congress was well aware that States might use tax credits to create discrimination against out-of-state producers or consumers of electricity. In its report on the bill that became Section 391, the Senate Finance Committee, specifically referring to the New Mexico tax, observed that the "credit normally benefits only domiciliaries of the taxing State since no credit is allowed for electricity produced within the State and consumed outside the State." S. Rep. No. 938, 94th Cong., 2d Sess., pt. I, at 437 (1976). The ultimate effect, as the Committee recognized, was that "the cost of the electricity to nondomiciliaries is normally increased by the cost the producer of the electricity must bear in paying the tax," while "the cost to domiciliaries . . . does not include the amount of the tax." *Id.* It was just that sort of inequality—whether achieved "directly or indirectly"—that Section 391 was enacted to stop.

Against this background, it seems self-evident that the New Hampshire tax scheme runs directly afoul of the prohibitions of Section 391: like the scheme in New Mexico, the New Hampshire tax provisions expose utilities conducting business elsewhere to higher tax burdens than if they conducted the same business in-state. To avoid the holding of *Arizona Public Service,* therefore, New Hampshire argues that the Nuclear Property Tax is not a tax "on or with respect to the generation or transmission of electricity" as required by the statute. N.H. Br. at 54-59. But, as the Special Master recognized (Final Report 18-19), the statute explicitly uses broad language to prohibit any discriminatory tax: indeed, the inclusion of the phrase "with respect to" in addition to the word "on" necessarily conveys an expansive congressional meaning, or it would be mere surplusage.[30] And it would be a very odd use of language to declare that a tax on property *defined* by its specific use in generating electricity (property "used in generating, producing, supplying, and distributing electric power or light")—and the value of which ($3.5 billion) depends directly on its use for that purpose—is anything other than a tax "with respect to" the generation of electricity.

The second sentence of Section 391 confirms that a cramped reading of that section would be out of place. For Congress was careful to specify that a tax is discriminatory "if it results, *either directly or indirectly,* in a greater tax burden on electricity which is generated and transmitted in interstate commerce than on electricity generated and transmitted in intrastate commerce" (emphasis added). This language requires that a court take full account of the tax burden, both direct and indirect, that electricity sold in interstate commerce is required to bear. A tax on property specifically designed and used for generating electricity is obviously part of the tax burden incurred in generating that electricity, at least "indirectly" if not "directly."

The loophole that New Hampshire seeks to create is also incompatible with Congress' evident purpose in Section 391. Were New Hampshire correct, it apparently would mean that New Mexico, following the decision in *Arizona Pub. Serv. Co. v. Snead,* could have simply repealed its electrical energy tax, imposed a property tax designed to raise the same amount, *allowed the same*

[30] The phrase "with respect" to" is a broad phrase—similar to the phrase "relates to," which the Court has recently described as "'deliberately expansive' language." *Ingersoll-Rand Co. v. McClendon,* 111 S. Ct. 478, 482 (1990) (quoting *Pilot Life Ins. Co. v. Dedeaux,* 481 U.S. 41, 46 (1987)).

credit (now for the property tax) against the local gross receipts tax, and successfuly gotten around the prohibitions of Section 391. Yet, there is absolutely no reason to think that Congress would have been willing to tolerate *that* discrimination, simply because it was achieved by altering the form of the tax. To the contrary, the use of phrases like "with respect to" and "directly and indirectly" suggests that Congress meant to prohibit discriminatory taxation relating to the generation of electricity, no matter what form it took.

II. THE PROPER REMEDY INCLUDES A REFUND OF THE SEABROOK TAX.

A. There Is No Basis for Making the Ruling in This Case Prospective Only.

New Hampshire contends that, even if its tax scheme violates the Commerce Clause or 15 U.S.C. § 391, retroactive relief is inappropriate. On the threshold issue—whether the ruling of this Court should apply to the past as well as the future—New Hampshire argues that any decision holding the New Hampshire tax scheme invalid should be deemed prospective only, under the decision in *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971). *See* N.H. Br. at 63-65. This argument is simply insupportable.

To begin with, as the Special Master pointed out (Final Report 39), there is substantial doubt about whether *Chevron* remains controlling authority on the choice-of-law issue. The divided opinions in *American Trucking Ass'ns v. Smith,* 496 U.S. 167 (1990), and in *James B. Beam Distilling Co. v. Georgia,* 111 S. Ct. 2439 (1991), make clear that it is now open to question whether a decision may *ever* be made prospective only—*i.e.,* not even applicable to the case in which it is announced—because such a decision has an "advisory" character. Indeed, in *American Trucking Ass'ns,* a majority of the Court expressed the view that, as a choice-of-law matter, the law determined by the decision in a case necessarily governs the conduct at issue in the case. *See* 496 U.S. at 200-01 (Scalia, J., concurring in the judgment); *id.* at 212-24 (Stevens, J., with whom Brennan, Marshall, & Blackmun, JJ., join, dissenting). If that view is now the law, then New Hampshire's *Chevron* argument founders on its own premise.[31]

In any event, even if *Chevron* is good law, New Hampshire cannot meet even the initial requirement set by that decision. The primary legal ground on which the New Hampshire tax scheme is invalid—the discriminatory, internally inconsistent linking of two local taxes through a credit provision—is anything but new. As we have shown, invalidity on this ground was more than merely "foreshadowed" (*Chevron,* 404 U.S. at 106) by federal law at the time that this tax scheme was enacted; invalidity was readily apparent from the repeated decisions of this Court striking down state tax schemes on precisely this ground. *See, e.g., Tyler Pipe; Armco v. Hardesty; Westinghouse Corp. v. Tully; Arizona Pub. Serv. Co. v. Snead.* Accordingly, as the Special Master concluded (Final Report 40-41), New Hampshire can have no plausible basis for pleading surprise at a ruling that its tax scheme is unlawful: it simply has no claim that such a ruling upset any legitimate reliance on prior authority.[32] New Hampshire therefore fails at the first step—as well

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[31] We note that, in *Harper v. Virginia Dep't of Taxation,* No. 91-794, the Court has pending before it issues regarding the prospectivity of decisions declaring tax statutes to be unconstitutional.

[32] Seeking support in *American Trucking Ass'ns v. Smith,* New Hampshire says that it "was entitled to rely on established precedent upholding property taxes and on the absence of any decision invalidating a nondiscriminatory income tax credit." N.H. Br. 65. The primary flaw in New Hampshire's tax scheme, however, is that it is *not* simply a property tax (it links two taxes through a credit) and its credit *is* discriminatory. Moreover, *Smith* cannot help New Hampshire, because the plurality there applied *Chevron* only after noting that the decision on which the Court relied had actually overruled prior authority. 496 U.S. at 179-80. There is no such departure from prior law in this case.

as later steps (*see* Final Report 41)—in seeking entry into the narrow class of cases (if it exists at all) in which courts may declare the law in a purely prospective manner.

B. The Appropriate Retroactive Relief Is a Refund of the Seabrook Tax.

New Hampshire also seeks to escape the award of retroactive relief by arguing that, under *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco,* 496 U.S. 18, 40 (1990), the Court need not order refunds of the Seabrook taxes paid (minus the increased business profits tax due upon striking the credit provision). N.H. Br. at 66-69. The Special Master properly concluded, however, that the remedy in this case should "put the parties back into the positions they would have held if New Hampshire had never adopted its unconstitutional tax scheme." Final Report 44. The Special Master, likewise, was correct in deciding that a refund, adjusted for credits taken, was the most appropriate means of retroactive relief.

We note, at the outset, that New Hampshire does not quarrel with the remedial standard employed by the Special Master: that is, to "put the parties back into the positions they would have held if New Hampshire had never adopted its unconstitutional tax scheme." *Ibid.* Its argument is simply that the Court should allow the State, rather than the Court, to decide (at least initially) what those "positions" would have been. But, as the Special Master pointed out, the legislature enacting the Seabrook Tax spoke to precisely that question: by including a nonseverability clause in the statute, it made clear that any assessment of the Seabrook Tax was conditioned upon—and could not exist without—the allowance of a credit for payment of that tax against liability for the state Business Profits Tax.

Contrary to the argument now made by the State, N.H. Br. at 69, the nonseverability clause does not address only the future and not the past. The inclusion of a nonseverability clause in a statute—an action that is more the exception than the rule[33]—reflects an overt legislative judgment that the two provisions must exist together or not at all. Because the grant of a discriminatory credit was unconstitutional from the moment that the Seabrook Tax took effect, retention of the Seabrook Tax revenues can be justified only if it can reasonably be said that the legislature in 1991 would have enacted that tax without the credit. But, if that had been the intention of the legislature—and an achievable result in light of the political realities of the time—then it appears obvious that the legislature would simply have left the tax and credit subject to the general severability clause. *See* note 33 *supra*. Instead, the legislature drafted a specific nonseverability clause saying just the opposite. *See Bowsher v. Synar,* 478 U.S. 714, 735-36 (1986) (where statute specifies the consequences of partial invalidation, such a provision is "fully operative as a law" and should be followed in preference to "creative and imaginative statutory surgery") (internal quotations omitted).[34]

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[33] Indeed, the legislation containing the Seabrook Tax and the accompanying credit has a separate provision declaring all provisions to be severable *except* for the Seabrook Tax and credit. 1991 N.H. Laws, c. 354:20.

[34] New Hampshire also argues that the combination of the Seabrook Tax and credit works "no actual discrimination" against "[u]tilities engaged in interstate commerce," which, New Hampshire says, actually were the principal "beneficiaries" of this scheme. N.H. Br. at 67. But, as an initial matter, New Hampshire rests this assertion on the hypothetical effects of the Seabrook Tax without the credit—precisely the unhinging of tax and credit that the New Hampshire legislature declared to be unacceptable. Moreover, the argument incorporates the same mistake that New Hampshire makes on the merits: as we have previously noted (*see* pages 24-25 *supra*), *all* Seabrook owners subject to tax on their business profits suffer the effects of the discriminatory structure of the statute, in varying degrees.

The decision in *McKesson* is not to the contrary. There, the Court simply held that, when a tax is declared to be discriminatory (and there is no basis for a prospective ruling), the due process clause requires that taxpayers be given "meaningful backward-looking relief." 496 U.S. at 31.[35] In *McKesson,* however—a case that involved an exemption from a tax on alcoholic beverages for certain beverages made from local products—there was concededly an open question whether the retroactive relief could take the form of an excision of the exemption or whether a refund (or some similar relief) was required, and the Court left that question for decision by the state courts on remand. In this case, by contrast, the legislature has already answered the question left open on remand in *McKesson*: it has declared that the tax and credit must be considered as "a unit." Final Report 43. If the taxpayers cannot take the credit in the past (and, because it is discriminatory, they cannot), then it is inconsistent with that declaration to say that the payments of the Seabrook Tax are to be treated as a separate, independent event for purposes of the remedy.

Although New Hampshire would plainly like to reconstruct these legislative determinations after-the-fact—perhaps as a lesson to taxpayers challenging discriminatory credits from which they receive some (though lesser) benefits—there is no good reason to allow it to do so. As the Special Master stated, "it reasonably should have been apparent to New Hampshire that its Seabrook Tax and credit scheme was of dubious constitutionality." Final Report 41. As a result, "[t]o the extent New Hampshire suffers hardships as a result of a retroactive decision, they are largely of its own making." Final Report 41. Indeed,

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[35] The Court in *McKesson* applied this principle to cases in which taxpayers were compelled to pay the taxes "under duress." The Special Master found that "[t]he Seabrook owners were 'under duress' to pay the Seabrook Tax when due and were relegated to postpayment refund action." Final Report 42.

insofar as the refund is brought about by the nonseverability clause, that is a perfectly appropriate consequence of a provision designed to reassure those owners with the greatest in-state business that they would not have to bear the general obligation (the Seabrook Tax) without at the same time gaining the advantages of the discriminatory offset (the credit). Against that background, it is too late now for New Hampshire to claim that the tax and credit were really unconnected all along.

C. The Eleventh Amendment Is No Bar to Refund Relief.

New Hampshire's final effort to escape the remedy of a refund relies on the Eleventh Amendment. N.H. Br. 69-74. New Hampshire briefly argues that the Eleventh Amendment would bar a refund in this case because, the State says, intervenors' rights "cannot exceed the rights they would have if they had been entitled to maintain an action in this Court in their own names." *Id.* at 72-73. But it is established law that the plaintiff States are entitled to the requested remedy—*i.e.*, to an order directing payment of a refund directly to the intervenor taxpayers—and that the Eleventh Amendment is no bar to such relief. That is precisely the relief that was awarded in *Maryland v. Louisiana,* 452 U.S. 456, 456-57 (1981) (entering decree ordering refunds be paid to the taxpayers), after the Court had rejected Louisiana's Eleventh Amendment objection to the suit. *Maryland v. Louisiana,* 451 U.S. at 745 n.21. This case is no different.

It is true that a State may not exploit its freedom from Eleventh Amendment limits to bring a suit that seeks only "to recover for injuries to specific individuals" rather than to vindicate its own interests. *Maryland v. Louisiana,* 451 U.S. at 745 n.21; *Hawaii v. Standard Oil Co.,* 405 U.S. 251, 258 n.12 (1972). Such a suit is a private suit in everything but name: the real parties in interest are the private individuals. But there is no such subterfuge here, for the plaintiff States have sued to vindicate *their own* interests—as ultimate purchasers of electricity and as sovereign representatives of all their residents who purchase electricity.[36] The relief sought vindicates those interests even though a discrete number of intervenors are the immediate beneficiaries—just as in *Maryland v. Louisiana, supra,* and (for example) in *Arizona v. California,* 460 U.S. 605, 613-14 (1983) (allowing intervention of Indian Tribes over Eleventh Amendment objection); 466 U.S. 144 (1984) (awarding water rights directly to the Tribes). Here, as in those cases, the State is entitled to relief that runs directly to private intervenors as a means of indirectly protecting its own interests (in utility bills unaffected by a discriminatory tax). The Eleventh Amendment presents no obstacle to this relief.

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[36] New Hampshire also argues that the Eleventh Amendment is a bar because, as a matter of fact, the utilities are not "merely a conduit to consumers." N.H. Br. at 71. But the State made no such factual argument before the Special Master—other than to assert, in a footnote, that "before January 19, 1993, no Connecticut consumers, including the State government, will pay any Nuclear Property Tax." Answering Brief of New Hampshire Before the Special Master at 86 n.35. Having chosen not to press a more general argument before the Special Master, New Hampshire can hardly complain that the Master did not accept it. Moreover, even if it were not tardy, the argument simply ignores the fact that, despite differing time periods, consumers burdened in the past by increased utility costs attributable to the Seabrook Tax are seeking to benefit in the future by decreased utility costs attributable to the refund of that tax.

CONCLUSION

The Court should enter judgment for intervenors and against the defendant on their claims under the Commerce Clause and Section 391.

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