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**OFFICIAL TRANSCRIPT  
PROCEEDINGS BEFORE  
THE SUPREME COURT  
OF THE  
UNITED STATES**

**CAPTION:** SHELL OIL COMPANY, Appellant, v.  
IOWA DEPARTMENT OF REVENUE

**CASE NO:** 87-984

**PLACE:** WASHINGTON, D.C.

**DATE:** October 4, 1988

**PAGES:** 1 - 45

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IN THE SUPREME COURT OF THE UNITED STATES

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SHELL OIL COMPANY :

Appellant :

V. : No. 87-984

IOWA DEPARTMENT OF REVENUE :

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Washington, D.C.

Tuesday, October 4, 1988

The above-titled matter came on for oral  
argument before the Supreme Court of the United States  
at 11:00 o'clock a.m.

1 APPEARANCES:

2

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4 on behalf of the Appellant.

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10 Washington, D.C., on behalf of the United States,

11 as amicus curiae, in support of Appellee.

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C O N T E N T S

|   | <u>PAGE</u> |
|---|-------------|
| <u>ORAL ARGUMENT OF</u>                 |             |
| KENNETH S. GELLER,                      |             |
| on behalf of the appellant              | 4           |
| HARRY M. GRIGER,                        |             |
| on behalf of the appellee               | 29          |
| LAWRENCE G. WALLACE,                    |             |
| as amicus curiae in support of appellee | 37          |
| <u>REBUTTAL ARGUMENT OF:</u>            |             |
| KENNETH S. GELLER,                      |             |
| on behalf of the appellant              | 43          |

1 (11:00 a.m.)

2 P R O C E E D I N G S

3 CHIEF JUSTICE REHNQUIST: We'll hear argument  
4 next on Number 87-984, Shell Oil Company versus the Iowa  
5 Department of Revenue.

6 We'll wait just a moment, Mr. Geller.

7 Very well. You may proceed whenever you're  
8 ready.

9 ORAL ARGUMENT OF KENNETH S. GELLER

10 ON BEHALF OF THE APPELLANT

11 MR. GELLER: Thank you, Mr. Chief Justice, and  
12 may it please the Court, the issue in this case is  
13 whether the State of Iowa may tax the income earned by  
14 Shell Oil Company in the extraction of oil and gas from  
15 the outer continental shelf.

16 Simply stated, Iowa requires Shell to take its  
17 OCS earnings into account in figuring out its Iowa  
18 income tax liability, with the result being that the  
19 more money Shell earns on the outer continental shelf,  
20 the more Iowa income tax it generally pays.

21 It's our position that State taxation of this  
22 sort is prohibited by the language, the legislative  
23 history, and the purposes and policies of the Outer  
24 Continental Shelf Lands Act, which demonstrate, we  
25 believe, that Congress meant to prohibit the States from

1 taxing any portion of OCS revenue.

2 Iowa, on the other hand, contends that the Act  
3 contains an implied exception for apportioned income  
4 taxes.

5 Let me begin by briefly explaining the  
6 background of this dispute. Shell engages in  
7 substantial exploration for oil and gas on the outer  
8 continental shelf, pursuant to Federal leases. Now,  
9 it's relatively easy for Shell to figure out its net  
10 income from these OCS operations, because the oil and  
11 gas has a definite and easily ascertainable fair market  
12 value at the wellhead, and Shell also knows what its  
13 expenses are in extracting the oil and gas from the  
14 shelf.

15 In fact, Shell has to figure out, make these  
16 precise calculations for a number of Federal purposes,  
17 such as the windfall profits tax, the oil depletion  
18 allowances, and most importantly, in figuring out the  
19 amount it owes to the Federal Government as royalties on  
20 these Federal leases.

21 Now, Shell also does business in Iowa, and as  
22 a result, it's subject to Iowa's corporate income tax.  
23 Now, Iowa, like virtually every State, determines the  
24 income tax liability for a multi-state business through  
25 use of a formula apportionment method. It starts with

1 the corporation's Federal income tax base, its net  
2 income for Federal income tax purposes, and it then  
3 subtracts from that Federal income tax amounts that it  
4 either can't Constitutionally tax, such as items that  
5 may not be part of the unitary business, or items that  
6 Congress by statute has prohibited it from taxing, such  
7 as, for example, the interest on Federal securities.

8 Now, what is left then is the Iowa income tax  
9 base. Then multiplies that by a percentage -- in most  
10 States, that percentage is based on three factors of  
11 payroll, property and sales. As the Court is aware from  
12 its decision in *Moorman*, Iowa uses a one factor sales  
13 formula with the numerator being sales in Iowa, and the  
14 denominator being sales everywhere. Then multiplies  
15 that Iowa income base by this fraction, and it comes up  
16 with the corporation's Iowa taxable income.

17 Now, when Shell computed its Iowa income for the  
18 years in question, it subtracted from its Federal income  
19 base the amounts it earned from the extraction of oil  
20 and gas from the outer continental shelf, and it did  
21 that based on the provisions of the Outer Continental  
22 Shelf Lands Act, which provide "State taxation laws  
23 shall not apply to the outer continental shelf."

24 And as the Court will know from the table  
25 reproduced at footnote seven at page 10 of our brief,

1 when Shell's OCS income was not subjected to the  
2 provisions of Iowa's income tax laws, it made a  
3 substantial difference in Shell's Iowa income tax  
4 liability.

5 Now, the State challenged the way in which --

6 QUESTION: Tell me again, Mr. Geller, how that  
7 computation was made. Shell has certain income which,  
8 from sales resulting from production in the OCS?

9 MR. GELLER: Not from sales, Mr. Chief Justice.

10 Shell has certain income that it earns on the  
11 shelf from the very act of extracting the oil and gas  
12 from the ocean floor and bringing it to the surface. It  
13 has a wellhead value. And Shell also knows --

14 QUESTION: But I wouldn't think that was  
15 income in the ordinary sense.

16 MR. GELLER: Well, it's not realized income  
17 for purposes of paying an income tax on it at that  
18 moment, but it is treated as a sales equivalent or  
19 income for a number of Federal purposes, as I said  
20 earlier, including the windfall profits tax and  
21 depletion allowances, and most importantly, figuring out  
22 the royalties it owes to the Federal Government, which  
23 is based not on any subsequent sales that may occur, but  
24 on the net wellhead value.

25 QUESTION: On the value --



1 MR. GELLER: The value of the oil at the  
2 shelf. That's correct.

3 That is the earning -- that is the amount that  
4 Shell claims it earns from its OCS operations. The  
5 wellhead value less whatever expenses were incurred in  
6 bringing that oil and gas to the surface. That is the  
7 amount that it claims --

8 QUESTION: So Iowa is telling it to figure  
9 your Iowa tax by putting Iowa sales as the numerator and  
10 all sales as a denominator?

11 MR. GELLER: Yes, and multiplying that by an  
12 income base that includes the amounts that I just  
13 referred to -- the amounts that Shell earns from the  
14 extraction of oil and gas on the outer continental shelf.

15 It's crucial that we're talking here about the  
16 income base -- what must be included in that base.

17 QUESTION: Okay, but if preparation of either  
18 the numerator or the denominator, do those OCS figures --

19 MR. GELLER: OCS -- well, as I said, Iowa uses  
20 a one-factor formula --

21 QUESTION: But listen to my question.

22 MR. GELLER: Yes, sir.

23 QUESTION: I'm asking you, in preparing the  
24 numerator and the denominator of sales over sales, do  
25 the OCS, outer continental shelf, values come into the

1 calculation of either of those two?

2 MR. GELLER: Yes, they do.

3 QUESTION: How?

4 MR. GELLER: They wouldn't come into the  
5 numerator, which is Iowa sales. They come into the  
6 denominator. Any sales that Shell makes on the shelf  
7 itself -- and it sells a small quantity of oil and gas  
8 on the shelf -- would be included in its everywhere  
9 sales, which would be in the denominator. Of course, we  
10 object to that as well, because we claim that what  
11 Congress meant to do in passing the statute is to  
12 require the States to simply ignore any OCS values.

13 QUESTION: But that isn't your primary  
14 objection.

15 MR. GELLER: Our primary objection is the use  
16 in the income base of the net wellhead value that Shell  
17 earns from the extraction of oil and gas from the outer  
18 continental shelf. That's what we object to.

19 QUESTION: And the net income base is Shell's  
20 net income everywhere, is that right?

21 MR. GELLER: The income base is Shell's net  
22 income everywhere, which we claim should not include its  
23 net income on the outer continental shelf.

24 QUESTION: Does that include net income in the  
25 East Indies and places like that?

1 MR. GELLER: In those states that require  
2 worldwide computations, it does, yes.

3 QUESTION: Even though there's no question, I  
4 suppose, that Iowa could not directly tax something that  
5 was produced in the East Indies.

6 MR. GELLER: That's correct.

7 On the other hand, there's no Federal statute,  
8 either, that tells them they can't do that, and we claim  
9 that there's a Federal statute here.

10 I think it's important in light of that  
11 statement, Mr. Chief Justice, to begin by emphasizing  
12 that this case is quite different from a number of other  
13 State income tax cases that the Court has wrestled with  
14 in recent years.

15 This case doesn't involve any Constitutional  
16 challenge to Iowa's apportionment method. Therefore,  
17 many of the arguments in Iowa's brief about nexus or  
18 extraterritorial taxation or its citations and reliance  
19 on cases like Moorman or Exxon v. Wisconsin are, we  
20 think, quite irrelevant here.

21 Iowa may well have a Constitutional power to  
22 tax the earnings that Shell makes on the outer  
23 continental shelf.

24 QUESTION: Mr. Geller, let me just get one  
25 little detail.

1           You don't disagree with the proposition that  
2 these activities on the outer continental shelf are part  
3 of the unitary business?

4           MR. GELLER: We don't dispute that, Justice  
5 Stevens.

6           What we contend is not that there's any  
7 Constitutional restriction on Iowa's power to tax what  
8 Shell earns on the outer continental shelf, but that  
9 Congress has added an additional restriction by statute,  
10 in order to protect and promote operations on an  
11 exclusively Federal enclave, the outer continental shelf.

12           We believe that this conclusion follows from  
13 three crucial pieces of evidence. And the first, of  
14 course, is the language of the statute itself. And As I  
15 mentioned a moment ago, Section 1333(a)(2) of Title 43  
16 provides -- and I quote -- "State taxation laws shall  
17 not apply to the outer continental shelf."

18           And this language is reinforced by section  
19 1333(a)(3) of the statute, which states that subsection  
20 (a)(2), which I just read to you, shall never be  
21 interpreted in such a way as to allow the States to  
22 claim any share of the revenues from OCS mineral  
23 production. But that of course is precisely what Iowa  
24 is trying to do here by insisting that Shell include its  
25 OCS earning in its Iowa income base.

1 QUESTION: Well, I guess the concern, Mr.  
2 Geller, is whether the statutory provisions are really  
3 directed toward taxes within the jurisdiction of the  
4 State, such as property taxes or excise taxes, severance  
5 taxes, and so forth.

6 MR. GELLER: Right. That is the dispute  
7 between us and Iowa.

8 QUESTION: Exactly. And it isn't all that  
9 clear to me that Congress had in mind prohibiting any  
10 reference in an apportionment formula to OCS wellhead  
11 value gas.

12 MR. GELLER: Well, we think that Congress --

13 QUESTION: For the objective of determining  
14 what income was earned in Iowa.

15 MR. GELLER: Well, we think, as I said, that  
16 there are three reasons why Congress did include a  
17 comprehensive prohibition on State income tax. The  
18 first, as I was just referring to, is the language of  
19 the statute, which is categorical. It talks about State  
20 taxation laws. It doesn't make any distinctions between  
21 jurisdiction based laws and apportioned income taxation.  
22 It speaks generally of State taxation laws.

23 And I think that the legislative history bears  
24 this out, Justice O'Connor. The legislative history is  
25 quite long, and contentious, and we've cited it. We've

1 discussed it in our brief. Congress gave a lot of  
2 thought to what it was doing here. It seems to us that  
3 there are two salient points that bear repeating about  
4 the legislative history.

5 The first is that bill after bill after bill  
6 was introduced in Congress, during the course of the  
7 debates, to give the States some share of OCS revenues,  
8 no matter how modest. Every one of these attempts was  
9 rejected. Legislative leaders in both Houses --

10 QUESTION: All of the States, or just coastal  
11 States?

12 MR. GELLER: Well, Justice Kennedy, the focus,  
13 obviously, was on the coastal States, because the  
14 coastal States had been the prime beneficiaries under  
15 the prior system, whereby the States viewed the outer  
16 continental shelf as their own land.

17 Decisions of this Court between 1947 and 1950  
18 had held that the OCS was in fact not State land, but  
19 exclusively Federal land. And therefore, much of the  
20 debates in the legislative history were attempts by the  
21 coastal States to reassert the jurisdiction that they  
22 had previously exercised. But every one of those  
23 attempts was beaten back.

24 And of course, if we are right that Congress  
25 comprehensively prohibited the States from imposing any

1 income tax, any tax whatsoever, including income tax,  
2 then of course it serves to reason that that prohibition  
3 would apply to all States, and not just the coastal  
4 States.

5 QUESTION: Well, but you say "the States", and  
6 these other States had perhaps a basis or a nexus for a  
7 direct tax, and not just including it in an  
8 apportionment formula.

9 MR. GELLER: That's correct.

10 But it seems to us crucial that at no point in  
11 the legislative history -- at no point, and Iowa has not  
12 been able to cite to any -- was there a discussion only  
13 of jurisdiction based taxes.

14 Congress spoke of all State taxation, and in  
15 fact the only mention in the legislative history that is  
16 at all relevant to the question of apportioned income  
17 taxation points our way. Just as we pointed out in our  
18 brief, Senator Long of Louisiana specifically said on a  
19 number of occasions that if the statute passed as it was  
20 drafted --and it ultimately did pass as it was drafted  
21 -- that would mean that the States could not impose a  
22 tax on corporate profits.

23 He didn't --

24 QUESTION: That surely doesn't speak precisely  
25 to this question.

1 MR. GELLER: Well, I think, Mr. Chief Justice,  
2 that it's awfully close to this question.

3 We're dealing here with a tax on corporate  
4 profits. That's precisely what Iowa suggests is not  
5 covered by the statute.

6 QUESTION: But that's probably why we first  
7 turned to the language of the statute itself, and only as  
8 a last resort to comments on the Floor, because they are  
9 seldom very precise, and certainly this one does not  
10 strike me as hitting the nail on the head.

11 MR. GELLER: Well, it does refer to a tax on  
12 corporate profits, which is what we're dealing with  
13 here, and which is what Iowa suggests is not covered.

14 QUESTION: Well, it was also made by an  
15 opponent to the legislation, Mr. Geller.

16 MR. GELLER: It was made by someone who  
17 opposed the legislation, that's true.

18 QUESTION: And we don't often place great  
19 reliance on that kind of a remark.

20 MR. GELLER: Well, we're not asking the Court  
21 to place great reliance on it. But it is the only  
22 statement in the legislative history that focuses on the  
23 precise issue in this case. And more important than  
24 that, no Member of Congress expressed any disagreement  
25 with what Senator Long said.



1 QUESTION: In the metaphysics of the tax law,  
2 this really isn't a tax on OCS profits, is it?

3 MR. GELLER: Well, in terms of Constitutional  
4 objections to apportioned income taxes, this Court has  
5 said that what an apportioned income tax attempts to do  
6 is to figure out how much money a corporation has made  
7 in the State and to that extent of the Constitutional  
8 matter, we're not suggesting it is a tax on the OCS.

9 But there are two things to be said about  
10 that, Justice Kennedy. The first is that the statute  
11 doesn't say "State taxation laws shall not apply on the  
12 outer continental shelf", it says "State taxation laws  
13 shall not apply to the outer continental shelf". It  
14 seems to us that what Congress was getting at is that  
15 they didn't want the States to tax any activities that  
16 occurred on the outer continental shelf, and in any  
17 meaningful sense of the term, it seems to us, Congress  
18 meant to say that if profits were made on the outer  
19 continental -- after all, let me answer it this way.

20 Congress knew that profits were going -- at  
21 least hoped -- profits were going to be made on the  
22 outer continental shelf. That's how it attempted to  
23 encourage companies to go out and develop the outer  
24 continental shelf.

25 Now, it's crystal clear from the legislative

1 history -- and Iowa doesn't dispute this -- that  
2 Congress said, we do not want the States to grab any  
3 share of those profits, through a severance tax, through  
4 a sales tax, through an excise tax, through a property  
5 tax, or even through an unapportioned income tax.

6           So the question really becomes why would  
7 Congress have meant to make an exception for apportioned  
8 income taxes, if the result of allowing the States to  
9 impose apportioned income taxes would be the same as  
10 allowing them to impose these other types of taxes,  
11 which is to make operations on the shelf less  
12 profitable, which they clearly do.

13           It's undisputed in this case, as the figures I  
14 referred to earlier suggest, that the more profit that a  
15 company makes on the outer continental shelf, the more  
16 State tax it has to pay. Therefore, operations on the  
17 outer continental shelf are less profitable. If they're  
18 less profitable because the States impose a severance  
19 tax, or an excise tax, or a sales tax, Congress said  
20 they can't do it.

21           The question remains, given the policies of  
22 the Act, which were to encourage development on the  
23 shelf, by in fact immunizing the income earned out  
24 there, and to maximize Federal revenues, why would  
25 Congress have meant to exclude this one type of

1 taxation, apportioned income taxation, from the universe  
2 of taxes that they meant to prohibit the States from  
3 enforcing as to OCS revenues?

4 Now, Iowa never explains why. It never  
5 explains why its theory is consistent with the  
6 categorical language of the statute, which says State  
7 taxation laws shall not apply to the outer continental  
8 shelf --

9 QUESTION: Well, its theory, of course, is  
10 that it's only taxing income in the State. That's its  
11 theory.

12 MR. GELLER: That is its theory, Justice  
13 O'Connor. And I think it's faulty for the reason that  
14 it relies heavily on Constitutional notions.

15 We're not suggesting that Iowa is taxing  
16 income on the shelf for purposes of some claim that they  
17 don't have nexus, or it's an extraterritorial type of  
18 taxation. But it seems to us that Iowa's playing word  
19 games with the Court by saying it's not taxing income on  
20 the shelf. It is unquestionably requiring all oil  
21 companies to include OCS profits in figuring out its  
22 State income tax.

23 When one considers what Congress intended to  
24 do in this statute, it's inconceivable --

25 QUESTION: Well, as a reference point to

1 determine what share belongs to Iowa, I guess.

2 MR. GELLER: That's true.

3 Now, what apportioned income taxation does, in  
4 effect, is to treat all of the States as if they were a  
5 single taxing entity. And what apportioned income  
6 taxation does is to require all of the income of a  
7 multi-State corporation to be amassed in one pie, and  
8 what apportionment essentially says is what slice, what  
9 size slice of that pie is each State entitled to.

10 But the question here is the antecedent one of  
11 what is to go into the pie. And we think what Congress  
12 clearly said is that this is an area of exclusive  
13 Federal concern. It's of no concern to the States, the  
14 profits that are made out there. None of that is to be  
15 included in the income pie that the States would then --

16 QUESTION: Mr. Geller, I guess under your  
17 theory you're saying it doesn't get into the pie at all,  
18 but it would at least be involved in the sense that the  
19 sales of these petroleum products would go into  
20 computing both --the percentage figure, because those  
21 sales, when the stuff is ultimately sold, will be part  
22 of sales everywhere, wouldn't they?

23 MR. GELLER: No, our position --

24 QUESTION: I thought your view was the  
25 percentage wouldn't change, you just want to take it out

1 of the pie.

2 MR. GELLER: No, no, no. I thought I said in  
3 answer to the Chief Justice's question that what we're  
4 primarily concerned about is not including that amount  
5 in the income base.

6 QUESTION: I understand, income base.

7 MR. GELLER: For consistency, Justice Stevens,  
8 our position also is that any sales that occur on the  
9 shelf also have to be --

10 QUESTION: Oh, on sales -- I'm not talking  
11 about the sale on the shelf. I understand that's a  
12 small part of it.

13 I understand the petroleum extracted on the  
14 shelf, and then sent around the country, and ultimately  
15 sold in Iowa and everywhere else in the United States  
16 --those sales would still be included in the calculation  
17 of the percentage?

18 MR. GELLER: They would be included in the  
19 denominator.

20 QUESTION: And you don't say the statutory  
21 language forecloses that?

22 MR. GELLER: Not at all. And I think one of  
23 the ways in which Iowa has attempted to discredit our  
24 position is by grossly overstating it, to suggest that  
25 we are saying that even those sales must be excluded

1 from the computations.

2 I think -- we've never taken that position.

3 QUESTION: I didn't take it as grossly  
4 overstating it. I took it as carrying it to its logical  
5 conclusion.

6 If you say that the objective was to prevent  
7 the States from cutting in on the exclusive Federal  
8 power to derive funds from the shelf, surely they cut in  
9 when whatever gas and oil you get from the shelf can be  
10 taxed as soon as it's sold on the mainland.

11 MR. GELLER: I don't think so, Justice Scalia,  
12 for the following reason. We have to look at what  
13 Congress meant to do in the statute.

14 This section 1331(a)(3) is quite clear as to  
15 the extent of the immunity that Congress meant to grant  
16 here. And what they said is that the States are not to  
17 claim any interest in any revenues from the natural  
18 resources from the shelf.

19 Now, we think that means that when the profit  
20 is earned by extracting the oil and gas from the shelf,  
21 and income is earned, that is the amount that is  
22 excluded from the State tax computations.

23 Now, Congress did not say -- and it wouldn't  
24 have been consistent with what it was trying to do here  
25 -- that this oil and gas would be given an immunity as

1 it went through life, if it was turned into some other  
2 product, like petroleum, and it was subject to some  
3 transaction in some State, and the transaction tax was  
4 generally imposed in that State, it would make no sense,  
5 given the purposes here, to carry the immunity that far.

6 QUESTION: The point is, that you're not  
7 drawing the line simply on the basis of what the  
8 economic reality is.

9 MR. GELLER: We are drawing the line on the  
10 basis, we think, of what Congress meant to say, which is  
11 if you earn income on the outer continental shelf, from  
12 the extraction of oil and gas, that income is immunized  
13 from State taxation.

14 Now, any amount earned by the sale by some  
15 unrelated third party in Montana or Missouri --

16 QUESTION: Or by you, in Montana or Missouri.

17 MR. GELLER: Or by us.

18 QUESTION: If you carted it yourself and sold  
19 it in Montana, you'd still pay a sales tax?

20 MR. GELLER: We would still pay -- just like  
21 anyone else, Justice Scalia would pay a sales tax in  
22 that State for selling that product.

23 QUESTION: And the economic reality of that is  
24 that it renders the gas and oil that you take off the  
25 shelf somewhat less valuable than it otherwise would be.

1 MR. GELLER: I would think it would be de  
2 minimus given what Congress was trying to -- first of  
3 all there would be severe bookkeeping problems because  
4 it is impossible to trace oil which is fungible.

5 But what Congress had in mind is that the  
6 increment of income earned from the extraction of oil  
7 and gas on the shelf -- which is easily determinable,  
8 and it all accrues on the shelf itself -- is what is not  
9 to be included in the State income tax base. All of  
10 that income is earned on an exclusively Federal  
11 enclave. It's not a transaction tax such as you're  
12 referring to now, which the States generally can tax  
13 because it occurs within their jurisdiction and they  
14 generally tax transactions of that sort.

15 We're dealing with something quite different  
16 here.

17 Now, Iowa's position, as I believe Justice  
18 O'Connor referred to earlier, is to suggest that the  
19 statute only involves jurisdiction-based taxes. Now,  
20 there are a number of problems, we think, with that  
21 position.

22 The first, of course, is that it render the  
23 statute largely superfluous and redundant. After all,  
24 there would have been no reason to pass a statute to  
25 prevent the States from imposing jurisdiction-based



1 taxes on the OCS. This Court had held in a series of  
2 cases between 1947 and 1950 that the OCS was an area of  
3 exclusive Federal jurisdiction. Therefore, the Due  
4 Process clause and the Commerce clause already prevented  
5 the States from imposing any jurisdiction-based taxes on  
6 the OCS.

7           So there really wouldn't have been any reason,  
8 if that had been Congress' intention, to pass a  
9 separate, two separate statutory provisions providing  
10 that the States could not impose jurisdiction based  
11 taxes on the OCS.

12           The second point that Iowa makes is, as I said  
13 earlier, a bit of a linguistic point. They suggest that  
14 even if Section 1333(a)(2) means what it seems to say,  
15 which is that State taxation laws shall not apply to the  
16 outer continental shelf, that they are not really  
17 "applying" their State taxation laws to the outer  
18 continental shelf.

19           And for this, they rely, as I said earlier, on  
20 a series of decisions from this Court involving  
21 Constitutional or Due Process objections. Now it's true  
22 that this Court has said in a number of cases that  
23 apportioned taxation generally doesn't violate the due  
24 process clause, because it's really meant only to  
25 measure in-State taxation. There's no sort of

1 extraterritorial taxation going on.

2 And we don't challenge Iowa's right to tax OCS  
3 revenues under the Constitution. We think Congress  
4 meant something more than that when it passed the  
5 statute.

6 We think that Congress didn't have to be  
7 satisfied with the "rough approximations" that occur  
8 under the Due Process laws when apportioned State income  
9 taxation is attacked as violating rules against  
10 extraterritorial taxation. Congress had something more  
11 in mind.

12 We believe it could require, and in our view  
13 it plainly did require, more precision than the  
14 Constitution requires. It required that the States not  
15 include any OCS values in figuring out their State  
16 income taxes, just as, for example, Congress in passing  
17 Section 3124(a) of Title 31 prohibited the States from  
18 including any income earned from Federal securities in  
19 the income base subject to State taxation.

20 QUESTION: Mr. Geller, does the Federal  
21 Government have oil leases on property that it owns,  
22 other than the OCS lands?

23 MR. GELLER: I don't believe so.

24 QUESTION: No Government public lands are  
25 subject to oil leases?

1 MR. GELLER: Well, of course the OCS is  
2 Government public lands.

3 QUESTION: I know.

4 No other Government public lands?

5 MR. GELLER: I don't know of any others, Mr.  
6 Chief Justice.

7 Now, as I said, there is to be this area of  
8 Federally protected income from the States. Iowa  
9 concedes it can't pass a severance tax, or a property  
10 tax, or an excise tax, or an unapportioned income tax,  
11 but it claims, though, that it can apply an apportioned  
12 income tax to OCS income, even though it has the same  
13 practical effect of making OCS operations --

14 QUESTION: Well, come to think of it, what  
15 about Elk Hills and Teapot Dome and some of those?

16 MR. GELLER: Those are lands within the United  
17 States, and they're subject to a whole different series  
18 of statutes, Mr. Chief Justice, such as the Mineral  
19 Leasing Act.

20 QUESTION: But in any of those, is there a  
21 prohibition against -- that could be interpreted as  
22 prohibiting the use of such -- profits from those such  
23 as Iowa makes here?

24 MR. GELLER: No, Congress followed a totally  
25 different scheme in those Federal area, Mr. Chief

1 Justice, because those are areas within the States, and  
2 in many cases, the States had a legitimate claim to what  
3 went on in those areas. Some of those areas had been  
4 ceded to the Federal Government.

5 Congress -- if one reads the legislative  
6 history of the OCSLA, it's quite clear that Congress  
7 wanted to take a totally different approach with the  
8 OCS, because it was an area that had never been part of  
9 the States. It was an exclusively Federal enclave.

10 And therefore, what Congress wanted to say is  
11 that the State -- it is irrelevant to State tax laws  
12 what happens out here. Money is going to be made out  
13 here, we want to immunize that from State taxation in  
14 order to encourage development on the shelf, and in  
15 order to maximize Federal revenues.

16 Now, Iowa never explains how its theory of  
17 State taxation laws shall not apply to the outer  
18 continental shelf is in any way consistent with those  
19 purposes. Iowa concedes that if money is made on the  
20 shelf, that company's State tax income, State income tax  
21 liability goes up and therefore makes OCS operations  
22 less profitable.

23 Iowa concedes that it can't make OCS  
24 operations less profitable by imposing any other sort of  
25 tax out there. But it never explains why it is

1 consistent with the policies of the OCSLA to make OCS  
2 operations less profitable by imposing an apportioned  
3 income tax.

4           It really can't be seriously suggested here  
5 that Iowa hasn't required Shell to include its OCS  
6 income in figuring out its Iowa income tax liability.  
7 Iowa concedes that it requires Shell to include its OCS  
8 profits in its Iowa income base, and the undisputed  
9 figures that I referred to earlier show that Shell has  
10 to pay more in Iowa income taxes simply because it's  
11 making a profit on the shelf.

12           And we think the conclusion is therefore  
13 inescapable that in any meaningful sense of the  
14 statutory terms, Iowa has applied its income tax laws to  
15 the OCS. Iowa doesn't dispute that the more income  
16 Shell makes on the OCS, it has to include the income in  
17 its Iowa calculations for figuring out its Iowa income  
18 tax, and as a result it has to pay more, ultimately, in  
19 Iowa income tax. It's inconceivable that that would not  
20 be within Congress' contemplation when it said that  
21 State taxation laws shall not apply to the outer  
22 continental shelf.

23           We therefore believe that the Court should  
24 reverse the judgement of the Iowa Supreme Court.

25           If there are no further questions, I'd like to

1 reserve the balance of my time.

2 CHIEF JUSTICE REHNQUIST: Thank you, Mr.  
3 Geller.

4 We'll hear now from you, Mr. Griger.

5 ORAL ARGUMENT OF HARRY M. GRIGER

6 ON BEHALF OF THE APPELLEE

7 MR. GRIGER: Mr. Chief Justice, and may it  
8 please the Court, my argument discusses three points as  
9 to why Iowa's apportioned tax is not in conflict with  
10 the Outer Continental Shelf Lands Act.

11 First, absent extraterritorial taxation that  
12 violates the Fourteenth Amendment's Due Process clause,  
13 or the Commerce clause, State unitary apportioned  
14 taxation is not the exercise of State political  
15 jurisdiction outside the taxing State, but only inside.

16 Second, 43 U.S.C. Section 1331(a) which is  
17 found on pages 94(a) to 95(a) of the appendix to the  
18 jurisdictional statement precludes State political  
19 jurisdiction in the outer continental shelf by a taxing  
20 State, but not inside the taxing State.

21 And third, the 1978 Outer Continental Shelf  
22 Amendments are inapplicable to this case.

23 With respect to my first point, the unitary  
24 business formal apportionment method is a method for  
25 division of multi-state unitary income within and

1 without the State. It is designed to tax that income  
2 which is reasonably attributable to the taxing State as  
3 a result of the taxpayers' activities that occur there.

4 Unlike separate accounting, it recognizes that  
5 there are unquantifiable factors of profitability which  
6 arise from the unitary business as a whole, rather than  
7 from merely any particular segment, and that these  
8 factors of profitability contribute as a whole to the  
9 earnings of the entire unitary income. Its design is to  
10 value the income-producing activities in the taxing  
11 State, not outside.

12 My second point is with respect to section  
13 1333, subparagraph (a), which obviously is a key statute  
14 in this case. We contend that the statute precludes  
15 State political jurisdiction over the shelf, but not off  
16 the shelf.

17 Section 1333(a), subparagraph (1) provides for  
18 exclusive Federal jurisdiction on the outer continental  
19 shelf, but such language does not preclude reasonable  
20 apportionment income attribution to the taxing State.

21 The second subsection, which is subsection  
22 (a), sub (2), sub (A), provides that applicable and not  
23 inconsistent adjacent State law is adopted as surrogate  
24 Federal law. Within the context of that paragraph that  
25 says that, the last sentence states that State taxation

1 laws shall not apply to the outer continental shelf.

2 Now, one who reads that for the first time  
3 could understandably get the impression that that simply  
4 means that adjacent State tax laws shall not be adopted  
5 as surrogate Federal law. However, one could also read  
6 the language to confirm that there is no State political  
7 jurisdiction to be exercised in the outer continental  
8 shelf.

9 The language does not preclude a State from  
10 exercising its taxing jurisdiction off the shelf, which  
11 has occurred in this case.

12 The legislative history with respect to this  
13 taxation language denotes that there was a battle in the  
14 Congress between proponents, primarily from Louisiana  
15 and from Texas who wanted to extend their territorial  
16 jurisdiction to the outer continental shelf to impose  
17 primarily their severance taxes there, and opponents of  
18 State taxation who resisted such extension as  
19 unconstitutional extraterritorial taxation.

20 Senator Cordon in explaining the conference  
21 bill to the Senate, stated that the language (inaudible)  
22 State taxation laws do not apply to the outer  
23 continental shelf really added nothing to the bill. It  
24 was already covered in other provisions of the statute  
25 with respect to absence of State political jurisdiction



1 on the outer continental shelf.

2           Indeed, this Court in the Gulf Offshore case  
3 stated with respect to the third subsection here,  
4 section 1333(a)(3), that provides that nothing in the  
5 prior subsection, which provides for adoption of  
6 adjacent State law as Federal law, can be used by a  
7 State to exercise jurisdiction over the outer  
8 continental shelf of itself precluded any State taxation  
9 laws from being extended to the outer continental shelf.

10           Therefore, the language "State taxation laws  
11 shall not apply to the outer continental shelf" really  
12 added nothing to the bill, but according to Senator  
13 Cordon, was insisted by the House conferees out of a  
14 superabundance of caution.

15           And my third point is that the 1978 Outer  
16 Continental Shelf Act Amendments are simply inapplicable  
17 to the issue in this case.

18           QUESTION: Excuse me, before you go on to the  
19 next point, isn't there a better explanation than it's  
20 just a superabundance of caution, to say it twice?

21           That phrase "State taxation laws shall not  
22 apply to the outer continental shelf" comes at the end  
23 of a paragraph that specifies at the beginning that the  
24 civil and criminal laws of each adjacent State now in  
25 effect or hereafter adopted are declared to be the law

1 of the United States for that portion.

2 So it follows, one could argue, on the basis  
3 of that, that all laws are either civil or criminal, and  
4 therefore the tax laws apply there. And it comes at the  
5 end of that paragraph, and it says "State taxation laws  
6 shall not apply."

7 MR. GRIGER: That is certainly one  
8 interpretation.

9 QUESTION: I wouldn't consider that  
10 particularly redundant. I would consider it eliminating  
11 what might otherwise be an implication of (2)(a) that  
12 State taxation laws of the adjacent States could apply.

13 MR. GRIGER: That's certainly an  
14 interpretation.

15 The language comes from a House amendment to  
16 the House bill by Representative Keating. And he wanted  
17 to confirm that the States will not extend their  
18 territorial jurisdiction through taxation to the outer  
19 continental shelf, and therefore he wanted that language  
20 in the Act. And they chose to place it in that  
21 particular paragraph.

22 QUESTION: Suppose the State didn't use an  
23 apportionment formula, but they just arrived at the  
24 income earned in the State by just counting up the  
25 actual sales of oil and gas in Iowa, and figuring out

1 what the income was from those sales.

2 And obviously, they would include in that  
3 calculation oil and gas that originated on the outer  
4 continental shelf that was sold in, say, Iowa.

5 Would that be legal? Where they expressly  
6 include OCS gas in figuring their, directly in figuring  
7 their income?

8 MR. GRIGER: I'm not sure I understand the  
9 question. Do you mean if we had a separate accounting  
10 computation of income in Iowa without regard to  
11 apportionment, attributing income?

12 QUESTION: Exactly.

13 MR. GRIGER: No, because we would be taxing  
14 too much. We would probably be arrogating income from  
15 outside the State without apportionment.

16 QUESTION: Well, that's one reason why it  
17 wouldn't be good, but how about the statute? Would it  
18 violate the statute to do it that way?

19 MR. GRIGER: We would be extraterritorially  
20 applying our tax laws --

21 QUESTION: You're just taxing sales made in  
22 Iowa.

23 MR. GRIGER: Sorry, Your Honor.

24 If we just would tax sales made in -- I  
25 misunderstood your original question.

1           If we just imposed a tax on sales made in  
2 Iowa, there is no problem, in my opinion, with violating  
3 the Outer Continental Shelf Act.

4           QUESTION: Even though everybody agrees that a  
5 large portion of the sales made in Iowa involved sales  
6 of outer continental shelf oil or (inaudible)?

7           MR. GRIGER: No, I don't see the problem.

8           We could impose a property tax, for example,  
9 on the storage of outer continental shelf oil or gas  
10 stored in the State. We could impose a sales tax or  
11 some sort of occupation tax on that particular oil and  
12 gas sold.

13           The key is don't discriminate against it. As  
14 long as we have a non-discriminatory tax, our  
15 (inaudible) is not on the outer continental shelf, it's  
16 in the State of Iowa.

17           QUESTION: If that's the case, you would think  
18 that a state voir would be right in this case.

19           MR. GRIGER: I agree, your Honor.

20           As a matter of fact, Mr. Geller has conceded,  
21 in page 6 of his reply brief, that Iowa could impose  
22 such a property tax in Iowa, impose that on outer  
23 continental shelf oil and gas.

24           The concepts are no different, because the  
25 problem is, you have a unitary business. And because

1 it's a unitary business, formula apportionment is  
2 generally an acceptable way of attributing the income  
3 within the State, recognizing that activities from the  
4 entire business contribute to the earning of income.

5 But what we are trying to do is simply  
6 attribute income in reasonable proportions to Shell's  
7 activities in Iowa, and as Mr. Geller has stated, they  
8 don't contend that we've done otherwise.

9 My third point is with respect to the 1978 OCS  
10 amendments. Those amendments were designed to procure a  
11 fair return to the Federal Government while at the same  
12 time be fair to oil producers in increasing funds for  
13 exploration.

14 Now, the problem that these amendments were  
15 dealing with was the cash bonus, fixed royalty method of  
16 leasing in the outer continental shelf by the Federal  
17 Government with huge front-end payments. These payments  
18 were so large that they literally kept down competition  
19 in the shelf for lease bidding. Only a few of the major  
20 oil companies could afford the bids, and indeed, the  
21 legislative history shows at the Senate hearings they  
22 complained -- even some of the majors complained, such  
23 as Humble, Standard Oil -- complained that the amounts  
24 that they had to pay in terms of the front-end costs  
25 were very high.

1           It also led to low bids. There was an example  
2 in the legislative history where one company bid  
3 \$144,000 for a tract that had a potential value of \$20  
4 million.

5           Finally, it kept small producers off the shelf  
6 entirely, because they couldn't afford the huge,  
7 front-end bids.

8           The Congressional response to that was to  
9 amend section 1337 to provide for alternative bidding,  
10 which is discussed by this Court in the Watt case. Now  
11 note that State taxes were never mentioned. They're not  
12 mentioned in the statute, the 1978 amendments, they're  
13 not mentioned in the legislative history, and OCS  
14 producers at this time had been paying apportioned State  
15 taxes. In fact, Shell had, as denoted on page 47 of  
16 the Joint Appendix.

17           Therefore, in conclusion, Shell's challenge to  
18 the makeup of the unitary net income base subject to  
19 apportionment as in conflict with the Outer Continental  
20 Shelf Lands Act should be rejected, and the decision of  
21 the Iowa Supreme Court should be affirmed.

22           CHIEF JUSTICE REHNQUIST: Thank you, Mr.  
23 Griger.

24           We'll hear now from you, Mr. Wallace.

25           ORAL ARGUMENT BY LAWRENCE G. WALLACE

1                   AMICUS CURIAE IN SUPPORT OF APPELLEE

2                   MR. WALLACE: Thank you, Mr. Chief Justice,  
3 and may it please the Court, our position in this case  
4 is uncomplicated. In our view, the fundamental and  
5 dispositive flaw in Petitioner's claim is that it is  
6 based and was based in the State courts solely on a  
7 Federal statute that does not address, and was not  
8 intended to address, the subject matter of Petitioner's  
9 claim.

10                   Certainly none of the statutory language on  
11 which Petitioner relies in terms speaks to the question  
12 of apportionment methods in the State taxation of the  
13 in-state income of a unitary business. We may assume,  
14 for purposes of this case, that the language that  
15 Congress enacted would suffice, and this is  
16 questionable, but we may assume it would suffice, to  
17 have some effect on that subject.

18                   If the legislative history clearly showed that  
19 that was what Congress intended -- but the conspicuous  
20 thing about the legislative history, for our purposes,  
21 is that no one discussed or even adverted to the  
22 question of apportionment methods in determining the  
23 amount of a unitary business' income that is properly  
24 attributable to its in-state activities for State income  
25 taxation.

1           QUESTION: Well, Mr. Wallace, I guess if the  
2 language is clear on its face, we don't get to the  
3 legislative history.

4           MR. WALLACE: If the language were clear on  
5 its face in support of Petitioner's claim, that is  
6 correct.

7           But the language does not, in our view, refer  
8 in any way in terms to the question of apportioning the  
9 income of the unitary business, for purposes of  
10 determining the amount attributable to its in-state  
11 activities. And that subject, having been omitted from  
12 the legislative history, it is a subject that the Court  
13 is familiar with.

14          QUESTION: Well, but it used broad language,  
15 "State taxation laws shall not apply".

16          MR. WALLACE: Yes, but this Court's decisions  
17 dealing with the subject of unitary taxation are all  
18 premised on the notion that the taxes are not being  
19 applied extraterritorially, to something outside the  
20 State's borders. It is just a method of more accurately  
21 determining how much of a unitary business' income is  
22 properly attributable to its in-state activities,  
23 because of what the Court has called the theoretical  
24 weaknesses of separate geographical accounting in trying  
25 to apportion the income of a unitary business, where it



1 would be subject to imprecisions and manipulation --  
2 these are words that the Court has used -- were it not  
3 considered as a unit and apportioned according to the  
4 common apportioned formula methods.

5 Now, that is a subject that has occupied tens  
6 of pages in the United States Courts. It's a subject of  
7 some complexity, and no one discussed it in the course  
8 of the legislative history of this statute.

9 Instead, the entire controversy in the  
10 evolution and enactment of the provisions of the Outer  
11 Continental Shelf Lands Act, that are at issue here,  
12 concern the question of the proper relation between  
13 Federal law and the law of the immediately adjacent  
14 State in territorial governance of the outer continental  
15 shelf, a question to which Congress turned in the wake  
16 of this Court's decisions, holding that that was  
17 Federal, rather than State, territory.

18 And with respect to the particular subject of  
19 income taxation, the controversy before Congress never  
20 extended beyond the question whether the adjacent State  
21 should be allowed to tax income from activities on the  
22 outer continental shelf as if those activities had  
23 occurred within the State itself. That is not what Iowa  
24 has done, and is not the question here.

25 And, I specifically include the one snippet of

1 the legislative history that Shell particularly relies  
2 on --Senator Long's statement on the Floor -- and I'm  
3 perfectly willing to look at it as quoted in the  
4 Appellant's blue brief, on the merits, page 31, at the  
5 bottom of the page of text.

6 Senator Long -- this is the fourth line from  
7 the bottom of that page -- Senator Long recognized that  
8 OCS lessees would be "subject neither to the State  
9 severance tax, property tax, nor the tax on corporate  
10 profits". For all that appears, all he was referring to  
11 were three categories of tax that proponents of  
12 alternative bills wanted the adjacent State to be able  
13 to apply directly to the outer continental shelf, as if  
14 that were part of their territory, as many States had  
15 treated it prior to this Court's decisions holding it to  
16 be Federal territory.

17 That was what the controversy was about  
18 --whether they should be allowed to exercise taxing  
19 jurisdiction over this territory by grant of that  
20 authority by Congress, whether the effect on the State  
21 power to tax that followed from this Court's decisions  
22 would be overruled by legislation. That was the  
23 controversy. It had nothing to do with the issue.

24 QUESTION: Mr. Wallace? Mr. Wallace, it is  
25 true, is it not, that the Iowa tax, being enforced or

1 imposed in this case, is a tax on Shell's corporate  
2 profits?

3 MR. WALLACE: That is correct. But in  
4 context, there's nothing to indicate that Senator Long  
5 was talking about anything other than a tax being  
6 imposed by the adjacent State, either a severance tax, a  
7 property tax, or an income tax, on the activities on the  
8 shelf, as if those were still to be considered part of  
9 the State's territory, subject to the State's  
10 jurisdiction.

11 So, our conclusion is that the Iowa Supreme  
12 Court correctly held that the Federal statute does not  
13 address the apportionment issue that was before that  
14 court, and that that issue therefore continues to be  
15 governed only by this Court's decisions under the Due  
16 Process and Commerce clauses, and by State law.

17 And I might say, about State law, that many of  
18 the States, including Iowa and Florida, whose case is  
19 being held for this one, in applying their apportionment  
20 formulas start, in basing the total income subject to  
21 the formula, with Federal taxable income. And that, we  
22 know from the Internal Revenue Service, includes income  
23 derived from all portions of United States territory,  
24 including Federal enclaves within the States. If oil is  
25 produced on an Indian reservation or a Federal petroleum

1 reserve, all of that would normally be included in the  
2 apportionment formula, and income derived from  
3 operations on the outer continental shelf would  
4 ordinarily be included.

5 So, this statute, in our view, does not  
6 address that question, and since no Constitutional claim  
7 has been raised, the judgement of the Supreme Court of  
8 Iowa should be affirmed.

9 CHIEF JUSTICE REHNQUIST: Thank you, Mr.  
10 Wallace.

11 Mr. Geller, you have two minutes remaining.

12 REBUTTAL ARGUMENT BY KENNETH S. GELLER

13 MR. GELLER: Just a few things, Mr. Chief  
14 Justice.

15 First, I'd like to address the statement that  
16 Justice Scalia made earlier about the possible  
17 interpretation of the phrase "State taxation laws shall  
18 not apply to the outer continental shelf".

19 Justice Scalia suggested that maybe that was  
20 simply meant to exclude State tax laws from the State  
21 laws that were being adopted as Federal law, as I  
22 understand it. But I think that that makes absolutely  
23 no sense, when you look at the legislative debates.

24 The whole purpose of the debates was over  
25 whether the States would be able to share in any OCS

1 revenues. That's crystal clear, that this was intended  
2 to be a restriction on the States. But if State tax  
3 laws had been adopted as Federal law, under the first  
4 part of Section 1333(a)(2), then the revenues from those  
5 State taxes would have gone to the Federal Government,  
6 not to the States, and those State taxes would have been  
7 administered by the Federal Government, not by the  
8 States.

9 So therefore, I think that reading of the  
10 State tax prohibition would make it a restriction on the  
11 powers of the Federal Government, not on the powers of  
12 the States, which makes very little sense. Congress  
13 must have had something more in mind than not adopting  
14 State tax laws as Federal law, I believe, when it passed  
15 the State tax prohibition in section 1333(a)(2).

16 Now, I didn't hear anything in Iowa's  
17 statements here today, or either from the Solicitor  
18 General, explaining why it would make any sense, given  
19 the policies and purposes of the Act, to allow the  
20 States to diminish OCS profits through this one form of  
21 State taxation. They have some arguments about there  
22 being nothing on the face of the statute about  
23 apportionment methods. Of course there's nothing on the  
24 face of the statute that talks about property taxes or  
25 severance taxes either.

1 As Justice O'Connor said, Congress spoke quite  
2 categorically. It said State taxation laws as a group.

3 QUESTION: Do you think a gross receipts tax  
4 in Iowa on all sales, including sales of petroleum and  
5 including petroleum from the OCS, would be valid under  
6 the --

7 MR. GELLER: Yes. We have said -- I think I  
8 said earlier in response to Justice Scalia's question,  
9 transaction-based taxes of this sort, that are imposed  
10 well after any profits are earned on the OCS, are not  
11 within the intent of Congress in passing this immunity.  
12 We don't suggest the statute goes that far.

13 Thank you.

14 CHIEF JUSTICE REHNQUIST: Thank you, Mr.  
15 Geller.

16 The case is submitted.

17 (Whereupon, at 11:50 o'clock a.m., the case  
18 in the above-titled matter was submitted.)

CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

#87-984 - SHELL OIL COMPANY, Appellant V. IOWA DEPARTMENT OF REVENUE

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BY Judy Freilicher

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