Appeal No. 04-0319 **Cir. Ct. No. 02CV003533**

WISCONSIN COURT OF APPEALS
DISTRICT IV

NORTHWEST AIRLINES, INC.,

PLAINTIFF-APPELLANT-CROSS-RESPONDENT,

V.

WISCONSIN DEPARTMENT OF REVENUE,

DEFENDANT-RESPONDENT-CROSS-APPELLANT,

MIDWEST AIRLINES, INC.,

INTERVENING DEFENDANT-RESPONDENT-CROSS-APPELLANT.

CERTIFICATION BY WISCONSIN COURT OF APPEALS

Before Dykman, Lundsten and Higginbotham, JJ.

This case presents issues of statewide and national importance involving the ability of the state to provide tax incentives for businesses to locate, upgrade, or remain in the state. This particular case involves the validity of Wisconsin property tax exemptions for qualifying airline carriers. The central issue is whether recent Wisconsin legislation creating these exemptions, which provide significant tax incentives to airline carriers that operate "hub facilities" in Wisconsin, is unconstitutional under the dormant Commerce Clause of the United

States Constitution. A significant threshold issue is whether Congress has foreclosed dormant Commerce Clause review by federal statute.

The resolution of this case will likely affect several pending cases.[1] More importantly, a decision will likely affect Wisconsin's ability to compete with other states in attracting business and industry. This case would appear to have far-reaching implications for both Wisconsin's economy and the development of Commerce Clause law nationwide.

The state tax provisions at issue, found in WIS. STAT. chs. 70 and 76, presently exempt Midwest Express and Air Wisconsin from paying an estimated $2.5 million in property taxes each year. The briefing in this case persuasively establishes that the resolution of this case is likely to affect Wisconsin's ability to continue to attract airline services in the state. The outcome is also likely to significantly impact the economy of the entire state for at least two reasons.

First, any loss of airline services negatively impacts the existing economic health of the state. Airline hub facilities within the state not only provide direct economic benefits to the state, such as airline-related jobs, but also foster business activity in general by providing more frequent and more direct flights, affording better opportunities for same-day returns or service geared to

[1] The Department of Revenue explains in its brief that constitutional challenges to statutes that provide significant tax exemptions to airlines are pending in seven other cases in Dane County: ***Northwest Airlines, Inc. v. DOR***, No. 03-CV-3239; ***Delta Air Lines, Inc. v. DOR***, No. 03-CV-3401; ***Comair, Inc. v. DOR***, No. 03-CV-3402; ***Atlantic Southeast Airlines, Inc. v. DOR***, No. 03-CV-3403; ***American Eagle Airlines, Inc. v. DOR***, No. 03-CV-3404; ***Meseba Aviation, Inc. v. DOR***, No. 03-CV-3405; and ***United Parcel Service Co. v. DOR***, No. 03-CV-3411.

local market needs, and increasing the ability to send packages after other courier services have completed daily pick-ups.

Second, the resolution of this case may have far-reaching implications for the future health of Wisconsin's economy. Legislatively created tax incentives for firms that do business in a state are a common mechanism for attracting and maintaining economic enterprises. A judicial determination that the exemptions at issue here violate the dormant Commerce Clause would seemingly apply to similar tax incentives in other contexts. Thus, for example, the resolution of this case may determine whether Wisconsin is able to successfully compete with other states in biotechnology enterprises by providing tax incentives to attract biotechnology firms. The circuit court, which struck down the exemptions as unconstitutional, says as much. The court reasoned: "[A]llowing the legislature of a State to validly separate businesses into two separate classes based solely on the amount of business they do in-state would entirely eviscerate the negative protections of the Commerce Clause."

Additionally, the resolution of this case stands to influence Commerce Clause law development on a national level. This appears to be an evolving area of law, and a number of states have similar aviation-related tax incentives. A number of other courts have weighed in on the topic, but no case appears to involve precisely the type of tax exemption at issue here.

Accordingly, we hereby certify this case to the Wisconsin Supreme Court for its review and determination pursuant to WIS. STAT. RULE 809.61.

BACKGROUND

In 2001, the Wisconsin legislature created WIS. STAT. § 70.11(42) (2003-04),[2] which exempted from general property taxes under WIS. STAT. ch. 70 any "[p]roperty owned by an air carrier company that operates a hub facility in this state, if the property is used in the operation of the air carrier company." 2001 Wis. Act 16, § 2110 (effective Sept. 1, 2001). Section 70.11(42)(a)2. defines a "hub facility" to mean:

> a. A facility at an airport from which an air carrier company operated at least 45 common carrier departing flights each weekday in the prior year and from which it transported passengers to at least 15 nonstop destinations, as defined by rule by the department of revenue, or transported cargo to nonstop destinations, as defined by rule by the department of revenue.
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> b. An airport or any combination of airports in this state from which an air carrier company cumulatively operated at least 20 common carrier departing flights each weekday in the prior year, if the air carrier company's headquarters, as defined by rule by the department of revenue, is in this state.

The Act also amended WIS. STAT. § 76.02(1) to exclude air carriers operating such hub facilities in this state from the property taxes set forth in WIS. STAT. ch. 76, referred to here as ad valorem taxes. *See* 2001 Wis. Act 16, § 2231 (effective Sept. 1, 2001). Prior to the enactment of 2001 Wis. Act 16, all air carriers operating in this state were subject to ad valorem taxes under ch. 76 in lieu of general property taxes under ch. 70, without regard to where their hub facilities were located.

[2] All references to the Wisconsin Statutes are to the 2003-04 version unless otherwise noted.

Two air carriers qualified as operating "hub facilities" in the state in 2001 and 2002. Midwest Express qualified under WIS. STAT. § 70.11(42)(a)2.a., and Air Wisconsin qualified under § 70.11(42)(a)2.b. In comparison, Northwest Airlines, an air carrier that did not qualify for a hub-facility exemption, was assessed over $1.5 million in WIS. STAT. ch. 76 ad valorem taxes in each of the years 2001 and 2002.

Northwest Airlines initiated this action against the Department of Revenue (DOR), seeking both a redetermination of its tax assessment and a declaratory judgment that the amended provisions of WIS. STAT. chs. 70 and 76 pertaining to taxation of air carriers violate the dormant Commerce Clause of the United States Constitution and/or the equal protection clause and the uniformity clause of the Wisconsin Constitution. The circuit court dismissed Northwest's redetermination claim because Northwest failed to comply with redetermination procedures under WIS. STAT. § 76.08. The court also determined that the tax exemptions violated the dormant Commerce Clause, severing the provisions from the pertinent tax scheme and granting Northwest forward-looking declaratory relief.

Northwest appealed the circuit court's decision on redetermination and severability. DOR cross-appealed, and Midwest Airlines intervened and cross-appealed. DOR and Midwest both argue in support of the constitutionality of the exemptions.[3]

[3] We note that part of the dispute may fall away, depending on whether Northwest complied with procedural requirements under WIS. STAT. § 76.08 in seeking a redetermination of its previous tax assessments. Regardless how the § 76.08 issue is resolved, the significant constitutional issues that this case raises remain with respect to the circuit court's declaratory ruling.

DISCUSSION

The Commerce Clause of the United States Constitution provides: "Congress shall have power ... [t]o regulate commerce ... among the several states ...." U.S. CONST. art. 1, § 8, cl. 3. While a literal reading of the Commerce Clause evinces a grant of power to Congress, "the Commerce Clause also directly limits the power of the States to discriminate against interstate commerce." ***Wyoming v. Oklahoma***, 502 U.S. 437, 454 (1992). This negative aspect of the Commerce Clause, commonly referred to as the "dormant" Commerce Clause, "prohibits economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors." ***Id.***

A four-part test has evolved for evaluating whether a tax provision violates the Commerce Clause. That test requires courts to consider whether: (1) the activity taxed has a substantial nexus with the taxing state; (2) the tax is fairly apportioned; (3) the tax does not discriminate against interstate commerce; and (4) the tax is fairly related to services provided by the state. ***Complete Auto Transit, Inc. v. Brady***, 430 U.S. 274, 279 (1977). The dispute here focuses on the third part of the test.

At the same time, Congress may act to foreclose the application of the dormant Commerce Clause in a particular area.[4]

> Once Congress acts, courts are not free to review state taxes or other regulations under the dormant Commerce Clause. When Congress has struck the balance it deems

[4] The foreclosure issue was not raised until after the circuit court's decision declaring the tax exemptions unconstitutional. However, the parties have briefed this issue, and DOR makes a persuasive case as to why the foreclosure issue should be addressed on appeal.

> appropriate, the courts are no longer needed to prevent States from burdening commerce, and it matters not that the courts would invalidate the state tax or regulation under the Commerce Clause in the absence of congressional action.

Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 154 (1982) (citation omitted). However, "Congress must manifest its unambiguous intent before a federal statute will be read to permit or to approve" a state law discriminating against interstate commerce. ***Wyoming***, 502 U.S. at 458.

DOR and Midwest contend that Congress has acted to permit the hub-facility exemptions at issue here by enacting 49 U.S.C. § 40116.[5] That statute provides, in relevant part:

> **(d) Unreasonable burdens and discrimination against interstate commerce.**
>
> ….
>
> (2)(A) A State, political subdivision of a State, or authority acting for a State or political subdivision may not do any of the following acts because those acts unreasonably burden and discriminate against interstate commerce:
>
> > (i) assess air carrier transportation property at a value that has a higher ratio to the true market value of the property than the ratio that the assessed value of other commercial and industrial property of the same type in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
> >
> > (ii) levy or collect a tax on an assessment that may not be made under clause (i) of this subparagraph.

[5] Although the arguments advanced by DOR and Midwest are not all the same, those arguments overlap substantially. Accordingly, we refer to their arguments together.

> (iii) levy or collect an ad valorem property tax on air carrier transportation property at a tax rate greater than the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
>
> (iv) levy or collect a tax, fee, or charge, first taking effect after August 23, 1994, exclusively upon any business located at a commercial service airport or operating as a permittee of such an airport other than a tax, fee, or charge wholly utilized for airport or aeronautical purposes.
>
> ….
>
> **(e) Other allowable taxes and charges.** Except as provided in subsection (d) of this section, a State or political subdivision of a State may levy or collect—
>
> (1) taxes (except those taxes enumerated in subsection (b) of this section), including property taxes, net income taxes, franchise taxes, and sales or use taxes on the sale of goods or services ….

DOR and Midwest argue that the hub-facility exemptions do not fall within any of the specifically prohibited practices listed in 49 U.S.C. § 40116(d)(2)(A) and are therefore explicitly authorized by 49 U.S.C. § 40116(e), regardless of any impact on interstate commerce. DOR and Midwest cite a number of cases foreclosing dormant Commerce Clause review in a variety of different, but related, factual situations. *See, e.g.*, ***Northwest Airlines, Inc. v. County of Kent***, 510 U.S. 355 (1994); ***Burbank-Glendale-Pasadena Airport Auth. v. City of Burbank***, 76 Cal. Rptr. 2d 297 (Ct. App. 1998); *see also* ***American Airlines, Inc. v. County of San Mateo***, 912 P.2d 1198 (Cal. 1996).

Northwest highlights the factual distinctions in the cases cited by DOR and Midwest, then argues that Congress has not manifested "unambiguous intent" to foreclose dormant Commerce Clause review of tax exemptions such as those at issue here. *See generally* ***Wyoming***, 502 U.S. at 458 (stating

"unambiguous intent" requirement). In short, the foreclosure of dormant Commerce Clause review in the circumstances here appears to present a novel issue of constitutional dimension.

Assuming that dormant Commerce Clause review is not foreclosed, Northwest contends that the hub-facility exemptions impermissibly favor Wisconsin-based air carriers over air carriers based outside Wisconsin. Northwest claims that the exemptions, on their face, discriminate against interstate commerce because they treat taxpayers who own the same class of property differently based upon where their hub facilities are located. Northwest further argues that both the purpose and effect of the exemptions constitute impermissible economic protectionism—that is, to give Wisconsin-based air carriers a competitive "home field" advantage—as Northwest believes is evinced by the careful tailoring of the definition of "hub facility" to apply only to Midwest and Air Wisconsin.

To support its argument, Northwest cites extensively to a Harvard Law Review article by Professor Peter Enrich. Enrich states:

> In light of [the] substantial body of case law, the Commerce Clause argument against a wide range of familiar business location incentives is straightforward. By their nature, such provisions offer benefits to businesses that locate in-state, benefits that are not available to those locating elsewhere. The undisguised purpose of such measures is to give an advantage to local activities and the local economy, both directly, by reducing the cost of doing business in the state, and indirectly, by expanding in-state demand for materials and labor. Their intended effect is to influence business decisions about where to site economic activity and to diminish the significance of nontax considerations in such decisions. Moreover, in most cases, location incentives facially distinguish between in-state and out-of-state activities in specifying the parameters of their applicability.

Peter D. Enrich, *Saving the States from Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 433 (1996) (footnote omitted). Based on Professor Enrich's observations, it seems that there is a disconnect between the proliferation of state tax incentives for business and the "straightforward" Commerce Clause argument against those incentives.

DOR and Midwest counter that the hub-facility exemptions do not favor intrastate commerce over interstate commerce because all of the air carriers involved operate both within and outside the state. Rather, they contend the exemptions represent a location incentive designed to encourage local development and to attract additional interstate commerce to this state. *See* ***Boston Stock Exch. v. State Tax Comm'n***, 429 U.S. 318, 336-37 (1977). DOR and Midwest claim that the exemptions are facially neutral with respect to interstate commerce because the exemptions do not increase an air carrier's tax burden based on its out-of-state activities, and any airline could qualify for an exemption by increasing its flights in and out of this state. They further contend that any incidental burden on interstate commerce is not "clearly excessive" in relation to the local benefits, applying a balancing test set forth in ***Pike v. Bruce Church, Inc.***, 397 U.S. 137, 142 (1970).

In sum, we certify this case because it presents significant constitutional questions that are likely to have far-reaching implications for Wisconsin's economy and that may also develop Commerce Clause law on a national level.