Washington Law Review

Volume 55 | Number 4

11-1-1980

Constitutional Law—The Scope of the Commerce Clause in International Commerce—Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434 (1979)

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CONSTITUTIONAL LAW—THE SCOPE OF THE COMMERCE CLAUSE IN INTERNATIONAL COMMERCE—*Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979).

The County of Los Angeles levied a nondiscriminatory ad valorem tax[1] on shipping containers[2] used exclusively in international commerce and located temporarily within the state.[3] These containers, owned by six Japanese shipping companies,[4] were based and registered in Japan where they were taxed upon their full value.[5] The County assessed a tax, apportioned on the basis of how long the containers were actually located in California.[6] In contrast, Japan does not tax similar American-owned containers entering Japan in foreign commerce.[7]

1. An ad valorem property tax is a tax levied as a percentage of assessed property value. The tax was imposed upon domestic and foreign property alike. The Court noted: "there is no evidence that California has treated Japanese containers differently from domestic containers for purposes of applying its property tax." Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434, 440–41 nn. 3 & 4 (1979).

2. The Court in *Japan Line* quoted Simon's definition of containers.

> A container is a permanent reusable article of transport equipment . . . durably made of metal, and equipped with doors for easy access to the goods and for repeated use. It is designed to facilitate the handling, loading, stowage aboard ship, carriage, discharge from ship, movement, and transfer of large numbers of packages simultaneously by mechanical means to minimize the cost and risks of manually processing each package. SIMON, THE LAW OF SHIPPING CONTAINERS, 5 J. Maritime L. & Com. 507, 513 (1974).

Japan Line, 441 U.S. at 436 n.1.

3. On appeal, the parties stipulated: "Each container is in constant transit save for time spent undergoing repair or awaiting loading and unloading of cargo . . . Although none of appellants' containers stays permanently in California, some are there at any given time; a container's average stay in the State is less than three weeks." *Japan Line*, 441 U.S. at 436–37.

4. The Japanese companies were Japan Line, Ltd., Kawasaki Kisen Kaisha, Ltd., Mitsui O.S.K. Lines, Ltd., Nippon Yusen Kaisha, Showa Line, Ltd., and Yamashita-Shinnihon Steamship Co.

5. The Japanese tax is described in the Guide to Japanese Taxes 1975–76, *Kaikei ShoHo Sha*, Tokyo, Japan, 30, *reprinted in*, Appellants' Reply Brief at 1a-2a, Appendix A, *Japan Line*, 441 U.S. 434.

> *Fixed Asset Tax*. Fixed assets tax is paid by the registered owner of land, buildings, ships or any other kinds of depreciable assets as of January 1 of each year to a municipality (in exceptional cases, to a municipality and to a prefecture). "Registered owner" means the person registered as an owner of such property in a fixed assets tax ledger maintained by a municipality. . . . .
>
> The annual tax rate is 1.4%. In some relatively poor municipalities the tax rate is higher than 1.4%, but it may not be higher than 2.1% in any case.

See also discussion of the tax in *Japan Line*, 441 U.S. at 452 n.17.

6. The Court in *Japan Line* explained:

> Property present in California on March 1 (the "lien date" under California law) of any year is subject to ad valorem property tax. Cal. Rev. & Tax. Code Ann. §§ 117, 405, 2192 (West 1970 and Supp. 1979). A number of appellants' containers were physically present in appellees' jurisdictions on the lien dates in 1970, 1971, and 1972; this number was fairly representative of the containers' "average presence" during each year.

Japan Line, 441 U.S. at 437.

7. *Id.*

The Japanese companies paid the taxes under protest and successfully sued for refund in the Superior Court for the County of Los Angeles.[8] The California court of appeal reversed the trial court's holding.[9] The California Supreme Court subsequently granted a hearing of the case and unanimously adopted the court of appeal's opinion.[10] On appeal, the United States Supreme Court in *Japan Line, Ltd. v. County of Los Angeles*,[11] struck down the tax, as applied, holding that it violated the commerce clause. In so doing, the Court created a new formula for evaluating the constitutionality of state taxes levied on instrumentalities of foreign commerce. It added two tests to the standards previously applied to state taxes on interstate commerce.[12]

By exempting containers in international commerce from local ad valorem property taxes, the *Japan Line* Court's interpretation of the commerce clause gives foreign merchants an advantage over their domestic competitors. The Court, lacking alternative grounds[13] for exempting foreign containers from the state tax, concluded that the commerce clause justifies such disparate treatment. Rather than adopting an interpretation of the commerce clause which is inconsistent with its purpose, the Court should have upheld the tax and left the difficult question of international tax policy to be resolved comprehensively in a more appropriate forum.

8. The superior court held that applying the property tax in derogation of the "home port doctrine" subjected international commerce to multiple taxation and thus was unconstitutional under the commerce clause of the Federal Constitution. *Id.* at 438.

9. Japan Line, Ltd. v. County of Los Angeles, 61 Cal. App. 3d 562, 132 Cal. Rptr. 531 (1976).

10. 20 Cal. 3d 180, 141 Cal. Rptr. 905, 571 P.2d 254 (1977).

11. 441 U.S. 434 (1979).

12. 441 U.S. at 446–51. *See* notes 17, 33–41 and accompanying text *infra*. *See also* 7 HASTINGS CONST. L.Q. 316 (1980).

13. The Court rejected the taxpayers' assertion that the tax contravened the Treaty of Friendship, Commerce and Navigation Between the United States and Japan (FCN), Apr. 2, 1953, [1953] 4 U.S.T. 2063, T.I.A.S. No. 2863 (providing that Japanese nationals residing in the United States may not be subjected to payment of taxes "more burdensome than those borne by" United States nationals, and according Japan "most favored nation" status). *Japan Line*, 441 U.S. at 439 n.3. It deemed "frivolous" the taxpayers' claim that the tax was prohibited by the General Agreement on Tariffs and Trade (GATT), 61 Stat. A18 (providing that "imported products" may not be subjected to heavier taxes, or to less favorable treatment, than like products of domestic origin). *Id.* at 439–40 n.4.

The court of appeal had rejected the taxpayers' arguments that the tax constituted an indirect "Duty of Tonnage" proscribed by the U.S. CONST. art. I, § 10, cl. 3, and "Imposts or Duties" proscribed by U.S. CONST. art. I, § 10, cl. 2, but the United States Supreme Court, in view of its disposition, did not reach these arguments. Neither did it rule on the taxpayers' due process challenge. *Japan Line*, 441 U.S. at 439–40 nn. 3 & 4.

The taxpayers asserted in brief that the tax was repugnant to the federal excise tax, the Customs Convention on Containers and the implementing Customs Regulations, the Tariff Act of 1930, various aviation treaties and agreements, and the supremacy clause. They also argued that the tax constituted a prohibited "transit fee," did not satisfy the "presence" test, was not fairly related to services rendered, was not fairly apportioned, and was discriminatory. Brief for Appellants at 28–49, *Japan Line*, 441 U.S. at 440–41.

I. BACKGROUND

The commerce clause[14] limits a state's power to tax. It provides that "Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States . . . . "

The commerce clause was a response to the chaotic economy which the Articles of Confederation produced. Seaboard states exacted taxes for the mere transit of goods, thereby increasing the cost to inland consumers. Hostile state restrictions, retaliatory trade regulations, and protective tariffs combined to proliferate state disharmony and Balkanization of the economy.[15] The commerce clause was designed to promote a national economy by granting Congress the right to regulate commerce. The clause serves as both a grant of federal power, and a restraint on state action which would burden commerce.[16]

The commerce clause has been interpreted to prohibit state taxes which "unduly burden"[17] interstate commerce, as, for example, by subjecting it to multiple taxation.[18] Thus, the Supreme Court has declared that taxes on interstate commerce must (1) have a substantial nexus with the state; (2) be fairly apportioned; (3) not discriminate against interstate commerce; and (4) be fairly related to the services provided by the state.[19]

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14. U.S. CONST. art. I, § 8, cl. 3.

15. THE FEDERALIST No. 22 (A. Hamilton). G. GUNTHER, CONSTITUTIONAL LAW: CASES AND MATERIALS 127 (9th ed. 1975 & Supp. 1979).

16. GUNTHER, *supra* note 15, at 127.

17. *See* Hellerstein, *State Taxation Under the Commerce Clause: An Historical Perspective*, 29 VAND. L. REV. 335, at 336, 344, 348 (1976). *See generally* J. HELLERSTEIN & W. HELLERSTEIN, STATE AND LOCAL TAXATION: CASES AND MATERIALS (1978).

18. *See, e.g.*, Evco v. Jones, 409 U.S. 91 (1972)(unapportioned state tax on activities in interstate commerce held to violate commerce clause because the receipts were subject to a potential double tax burden via levies in other states to which intrastate commerce was immune); J.D. Adams Mfg. Co. v. Storen, 304 U.S. 307 (1938)(unapportioned state income tax constituted a regulation of and burden upon interstate commerce in violation of commerce clause because it created a risk of multiple taxation). *Cf.* Central R.R. v. Pennsylvania, 370 U.S. 607 (1962)(dicta)(tax on full value upheld where tax situs was not established elsewhere, the Court observing that only multiple taxation of interstate operations offends the commerce clause); Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938)(dicta)(in upholding the validity of the tax at issue, the Court noted that local taxes, measured by gross receipts from interstate commerce, have often been declared unconstitutional when they subject interstate commerce to a double tax burden not imposed upon intrastate commerce). *But cf.* Moorman Mfg. Co. v. Blair, 437 U.S. 267 (1978)(Court upheld a state sales tax formula against a commerce clause challenge where duplicate taxation was not proven and where overlap would only arise in the event of mathematical imprecision in apportionment, which imprecision does not contravene the commerce clause).

19. This four element test for taxes upon interstate commerce was first set forth in Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977), and was recently affirmed in Department of Revenue v. Association of Wash. Stevedoring Cos., 435 U.S. 734 (1978).

Various states may impose taxes, based on the estimated actual "presence"[20] of goods in their jurisdictions.

Foreign commerce presents even greater risks of multiple taxation than commerce between the states. In interstate commerce, the risk of multiple taxation is controlled by the availability of recourse to the United States Supreme Court, which has the power to adjudicate between the states.[21] When more than one nation imposes taxes upon goods in international commerce, however, there is no analogous mutually acknowledged sovereign to oversee apportionment.[22] Because apportionment is difficult in the international context, the home port doctrine,[23] with its simple principle of a single taxation jurisdiction, appears attractive. Largely for this reason, the same courts that have abandoned the home port rule in taxation of interstate commerce have been reluctant to discard it in taxation of foreign, and particularly oceangoing commerce.[24]

Despite its ease of application, the home port doctrine cannot assure the absence of multiple taxation in international commerce. For example, an American court's decision that California has exclusive taxing jurisdiction over a vessel with its port of origin in that state[25] cannot prevent a foreign power from levying its own tax upon the ship.[26] Moreover, be-

20. Brief for Appellees on Motion to Dismiss or Affirm at 9. *See also Japan Line*, 441 U.S. at 445.

21. *Japan Line*, 441 U.S. at 446–47.

22. The International Court of Justice could regulate apportionment, but only in the unlikely event that rival taxing authorities would submit to its jurisdiction. *Id.* at 438, 447.

23. The "home port doctrine" originated in Hays v. Pacific Mail S.S. Co., 58 U.S. (17 How.) 596 (1855). In *Hays*, California sought to impose property taxes on oceangoing vessels that had their home port in New York and remained only briefly in California to unload and undergo repairs. Because the vessels were in California only temporarily, they were held to have no tax situs there. The Court decided that the home port of New York was the only state with authority to tax the ships. In Morgan v. Parham, 83 U.S. (16 Wall.) 471 (1872), the Court expanded the home port doctrine from a rule of situs to a test for determining when commerce was "burdened." *See* Clark, *Property Taxation of Foreign Goods and Enterprises—A Study in Inconsistency*, 4 PEPPERDINE L. REV. 39, 52 (1976); Comment, *Limitations on State Taxation of Foreign Commerce: The Contemporary Vitality of the Home-Port Doctrine*, 127 U. PENN. L. REV. 817 (1979).

24. *See, e.g.*, Braniff Airways, Inc. v. Nebraska State Bd. of Equalization, 347 U.S. 590 (1954) (approving apportioned tax on domestic aircraft, but distinguishing vessels "used to plow the open seas"); Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169, 173 (1949)(approving apportioned tax on barges navigating inland waterways, but "not reach[ing] the question of taxability of ocean carriage"); Pullman's Palace Car Co. v. Pennsylvania, 141 U.S. 18 (1891)(approving apportioned tax on interstate railroad rolling stock, but distinguishing oceangoing vessels). The Court in *Japan Line*, 441 U.S. at 442, cited these three cases.

25. The home port is the port where the vessel is registered. Comment, *Limitations on State Taxation of Foreign Commerce: The Contemporary Vitality of the Home-Port Doctrine*, 127 U. PENN. L. REV. 817, 819 (1979).

26. In Hays v. Pacific Mail S.S. Co., 58 U.S. (17 How.) 596 (1855), the Court admitted that the home port doctrine cannot prevent multiple taxation of interstate and foreign commerce.

cause the home port doctrine has no clear constitutional foundation,[27] some courts have labelled it "anachronistic"[28] and even "abandoned."[29] With the traditional rule subject to such criticism, the proper standard for evaluating state taxation of instrumentalities of foreign commerce was unclear when *Japan Line* came before the Court.

II. CONTENTIONS AND COURT'S REASONING

The parties raised two principal issues. The taxpayers first argued that the containers should be subject to taxation only in their home port, Japan.[30] The County responded that the home port doctrine established merely a rule that taxes can be assessed by the jurisdiction in which the taxed property has situs. Such a rule, the County said, would not foreclose its taxation of containers which had actual situs in California.[31] The Court questioned the vitality of the home port doctrine, but found no need to reach that issue.[32]

The taxpayers further insisted that the concept of tax apportionment, which prevailed in interstate commerce, could not readily be translated into the context of foreign commerce, because it was neither feasible in practice nor consistent with international custom.[33] The County, on the other hand, defended the tax on the grounds that it met the commerce

27. *Japan Line*, 441 U.S. at 443. The home port doctrine has no constitutional source. It is based on common law jurisdiction to tax. *See* Note, *State Taxation of Foreign Aircraft Used in Foreign Commerce*, 49 CALIF. L. REV. 968, 969–71 (1961).

28. *Japan Line*, 441 U.S. at 443 (citing Northwest Airlines, Inc. v. Minnesota, 322 U.S. 292, 320 (1944)(Stone, C.J., dissenting)). In Sea-Land Serv., Inc. v. County of Alameda, 117 Cal.2d 448, 528 P.2d 56, 66 (1974), the court also described the home port doctrine as "anachronistic." The *Sea-Land* court observed that the United States Supreme Court's decision in Northwest Airlines, Inc. v. Minnesota, 322 U.S. 292 (1944), which permittted the "home port" to tax on full value because tax situs had not been established elsewhere, "cannot be read as supporting the home port doctrine." (Other citations omitted.) *Sea-Land*, 528 P.2d at 66 n.14.

29. Northwest Airlines, Inc. v. Minnesota, 322 U.S. at 320 (Stone, C.J., dissenting).

30. Brief for Appellants at 22–27. Appellants argued that the Court in Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169 (1949), and in Pullman's Palace Car Co. v. Pennsylvania, 141 U.S. 18 (1891), had been "careful not to abrogate the validity of the 'Home Port' rule in the case of instrumentalities used exclusively in foreign commerce." Brief for Appellants at 23. In fact, the Court in both cases had distinguished "oceangoing" commerce. *See* note 24 *supra*.

31. Brief for Appellees on Motion to Dismiss or Affirm at 10–11, *Japan Line*, 441 U.S. 434.

32. *Japan Line*, 441 U.S. at 443–44.

33. Brief for Appellants at 24–25, *Japan Line*, 441 U.S. 434. Specifically discussing international custom, appellants explained: "[i]t has been accepted by a multitude of foreign nations, which likewise exempt foreign vessels, ships' gear, and other integral parts of the vessel from taxation in their respective jurisdictions on the basis that other nations follow the same or similar concepts." *Id.* Appellants cited Zenith Radio Corp. v. United States, 437 U.S. 433 (1978), as demonstrating the importance of this "reliance interest." In addition, the *Japan Line* court noted: "[i]f an instrumentality of commerce is domiciled abroad, the country of domicile may have the right, consistent with the custom of nations, to impose a tax on its full value." *Japan Line*, 441 U.S. at 447.

clause test which had thus far been applied to interstate and foreign commerce.[34] The County emphasized that a single standard for interstate and foreign commerce would secure "equality" between domestic and foreign taxpayers and uniformity without impairing the federal government's ability to "fine tune" commercial relations with foreign governments.[35] Furthermore, the County argued that it was entitled to compensation for services, such as fire and police protection, which were extended to the stored containers.[36]

The Court invalidated the tax under the commerce clause,[37] declaring that a tax on instrumentalities of international commerce[38] must meet not only the four tests imposed in interstate commerce,[39] but two additional requirements. First, a tax on foreign commerce may be struck down if it raises a "substantial risk of international multiple taxation."[40] The Court emphasized that the California tax created more than a risk of multiple taxation; it created multiple taxation in fact.[41] Second, a tax must not prevent the federal government from "speaking with one voice" when regu-

34. *Japan Line,* 441 U.S. at 445. Appellees cited two state supreme court opinions, Canadian Pac. R.R. v. King County, 90 Wash. 38, 155 P.2d 416 (1916), and Sea-Land Serv., Inc. v. County of Alameda, 12 Cal. 3d 772, 117 Cal. Rptr. 448, 528 P.2d 56 (1974), to support this position. Appellees' Motion to Dismiss or Affirm at 12. In *Canadian Pacific,* the Washington court applied the interstate commerce taxability tests of Pullman's Palace Car Co. v. Pennsylvania, 141 U.S. 18 (1891), to foreign-owned railroad cars. In *Sea-Land,* the California court upheld an apportioned property tax on cargo shipping containers used in both interstate and foreign commerce.

Appellees also relied upon Zee Toys, Inc. v. County of Los Angeles, 85 Cal. App. 3d 763, 149 Cal. Rptr. 750 (1978)(*restored to the calendar for reargument,* 48 U.S.L.W. 3698), where the California court of appeal, citing Boston Stock Exch. v. State Tax. Comm'r, 429 U.S. 318 (1977), as authority, struck down as a violation of the commerce clause an ad valorem tax exemption which discriminated against interstate commerce in favor of foreign commerce. Appellees' Supplemental Brief at 1–3.

35. Appellees' Motion to Dismiss or Affirm at 12–13.

36. *Japan Line,* 441 U.S. at 445, 456–57. Services for which the property tax was collected, included "not only police and fire protection, but the benefits of a trained work force and the advantages of a civilized society." *Id.* at 445. *See also* Appellees' Motion to Dismiss or Affirm at 8 (noting, in addition, maintenance of roads).

37. *Japan Line,* 441 U.S. at 445–54. The Court did not expressly discuss the supremacy clause, though it declared the "desirability of uniform treatment of containers." *Id.* at 452.

38. The Court in *Japan Line* stressed that "[t]he question here is a . . . narrow one, that is, whether instrumentalities of commerce that are owned, based, and registered abroad and that are used exclusively in international commerce, may be subjected to apportioned ad valorem property taxation by a State." *Id.* at 444.

39. *Id.* at 445–51. *See* note 19 and accompany text *supra.* The Court assumed, arguendo, that the tax met the interstate commerce requirements. *Japan Line,* 441 U.S. at 451.

40. *Id.* at 451. The Court's formulation is phrased in terms of a substantial *risk* of multiple taxation; yet, the Court specifically limited its holding to cases where multiple taxation existed in fact. *Id.* at 452 n.17. Consequently, it is not clear what standards will apply to taxes presenting only a risk of multiple taxation.

41. *Id.* at 452.

lating commercial relations with foreign governments.[42] The Court concluded that the tax raised such an obstacle, stating that federal uniformity in this area was desirable.[43] Moreover, there was a risk of retaliation by foreign taxing authorities,[44] and if other states decided to impose similar taxes, instrumentalities of international commerce would be exposed to varying degrees of multiple taxation.[45]

The Court acknowledged the force of the County's arguments as to its uncompensated services[46] and discrimination against domestic taxpayers,[47] but stated that such claims were directed to the "wrong forum."[48] It rejected the County's argument that "any multiple taxation created by California's tax can be cured by congressional action or by international agreement."[49] The Court viewed these proposed alternatives as, in effect, a concession by the County that a uniform federal rule was necessary; consequently, the Court declared that "California may not tell this Nation or Japan how to run their foreign policies."[50]

III. COMMERCE CLAUSE ANALYSIS: MISINTERPRETATION

According to the Supreme Court's decision in *Japan Line,* the commerce clause demands a more stringent analysis when foreign, rather than interstate commerce is at issue. The Court concluded that a tax on an instrumentality of foreign commerce is unconstitutional, even when it is apportioned and nondiscriminatory, if it "creates a substantial risk of international multiple taxation,"[51] or if it "prevents the Federal Government from 'speaking with one voice.' "[52] The description, however, is based on a questionable constitutional analysis[53] which may have long lasting and undesirable consequences.

42. *Id.* at 451.
43. *See* note 37 *supra.*
44. *Japan Line,* 441 U.S. at 453.
45. *Id.*
46. *See* note 36 *supra.*
47. *Japan Line,* 441 U.S. at 457.
48. *Id.*
49. *Id.* at 454.
50. *Id.* at 455.
51. *Id.* at 451.
52. *Id.* at 449 (quoting Michelin Tire Corp. v. Wages, 423 U.S. 276, 285 (1976)).
53. The United States Supreme Court has recently chosen not to extend its *Japan Line* analysis into the context of apportioned state taxes on income from both domestic and foreign sources. Mobil Oil Corp. v. Commissioner of Taxes, 100 S. Ct. 1223 (1980).

A. *"Substantial Risk of International Multiple Taxation"*

The Supreme Court began its analysis with the observation: "[i]t is a commonplace of constitutional jurisprudence that multiple taxation may well be offensive to the Commerce Clause."[54] This statement is misleading as a general proposition and must be viewed in the context of the cases from which it was derived.[55] The cited cases do not prohibit multiple taxation as a per se violation of the commerce clause; rather, they prohibit a state from exacting more than its fair share. The cited cases required that property taxes on instrumentalities of commerce be apportioned among jurisdictions having a nexus to the property; consequently, neither the domicile state nor any other state may tax the full value of the property.

The cases cited by the Court stand for the proposition that a state which merely exacts an apportioned property tax does not violate the Constitution; rather, the domicile state which exacts more than its fair share places an unconstitutional burden on commerce. These cases are not squarely on point in an international commerce situation. If they were literally applied, they would lead the Court to conclude that Japan, the domicile jurisdiction that taxed the full value of the property, violated the commerce clause, not California.

The Court did not acknowledge that it was extending a doctrine derived in interstate commerce cases to an international commerce case. Instead, the Court explained that its previous approval of apportionment was based on its "ability to enforce full apportionment by all potential taxing bodies."[56] The commerce clause was designed to prevent *states* from placing unfair burdens on commerce. Any "unfair burden" in *Japan Line* was not the result of discriminatory state action, but was merely the result of Japan's decision to tax more than its fair share. The Court's inability to make Japan conform to our constitutional standards is irrelevant. The Court's duty is to ensure that states do not exact unfair taxes.[57] Nothing in the history of the commerce clause suggests that a nondiscriminatory, apportioned, ad valorem property tax which is fairly related to state services is the type of burden the Framers intended to eradicate.[58]

54. *Japan Line*, 441 U.S. at 446 (citations omitted).

55. Evco v. Jones, 409 U.S. 91, 94 (1972); Central R.R. v. Pennsylvania, 370 U.S. 607, 612 (1962); Standard Oil Co. v. Peck, 342 U.S. 382, 384–385 (1952); Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169, 174 (1949); J.D. Adams Mfg. Co. v. Storen, 304 U.S. 307, 311 (1938), all cited in *Japan Line*, 441 U.S. at 446.

56. *Japan Line*, 441 U.S. at 447.

57. *See* notes 15–18 and accompanying text *supra*.

58. *See* notes 15–20 and accompanying text *supra*. In Michelin Tire Corp. v. Wages, 423 U.S. at 288, the United States Supreme Court explained:

> To be sure, allowance of nondiscriminatory ad valorem property taxation may increase the cost

B. "Speaking with one Voice"

Alternatively, the Court rejected the California tax because it prevented the federal government from "speaking with one voice" in regulation of foreign commerce.[59] The Court cited the Customs Convention on Containers[60] as evidence of the desirability of uniformly treating containers moving in international commerce. It also pointed out that California's tax would create "an asymmetry in international maritime taxation,"[61] which might invite retaliatory taxes.[62]

It is unnecessary, however, to impose rigid federal uniformity in this case. Significantly, the Convention on Containers does not prescribe any rules for ad valorem property taxation. If its authors had intended to prescribe comprehensive federal regulations of container taxes, it seems likely they would have done so. Merely because uniform treatment of

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of goods purchased by 'inland' consumers. But as already noted, such taxation is the *quid pro quo* for benefits actually conferred by the taxing State. There is no reason why local taxpayers should subsidize the services used by the importer; ultimate consumers should pay for such services as police and fire protection accorded goods just as much as they should pay transportation costs associated with those goods (footnotes omitted).

For further discussion of *Michelin Tire*, *see* notes 67–73 and accompanying text *infra*.

The California Supreme Court has discussed the focus of the commerce clause. In Sea-Land Serv., Inc. v. County of Alameda, 117 Cal.2d 448, 528 P.2d 56, 67 (1974), the California court upheld the apportioned county tax on containers which were instrumentalities of both foreign and interstate commerce. In that opinion the court adopted the reasoning of Justice Traynor in his dissent in Scandinavian Airlines System, Inc. v. County of Los Angeles, 56 Cal.2d 11, 14 Cal. Rptr. 25, 363 P.2d 25 (1961). In *Scandinavian Airlines*, the court struck down an apportioned tax on airplanes flying international skies; the opinion, in effect, reaffirmed the home port doctrine. *Sea-Land*, 528 P.2d at 65. In *Sea-Land*, the court concluded that "any threat of multiple burdens imposed by *foreign* taxing authorities is irrelevant to the crucial issue of whether any *state* is discriminating against interstate or foreign commerce." *Sea-Land*, 528 P.2d at 67. It explained that merely because a state court lacks jurisdiction to compel independent nations to adopt a uniform nondiscriminatory system of taxation, "it does not follow that the states must forego the power to impose taxes that are not in themselves discriminatory." *Id.* (quoting *Scandinavian Airlines Sys.*, 363 P.2d at 45 (Traynor, J., dissenting)). *See* Japan Line, Ltd. v. County of Los Angeles, 20 Cal. 3d 180, 186, 141 Cal. Rptr. 905, 908, 571 P.2d 254, 257 (1977).

59. *See* note 52 *supra*.

60. *Japan Line*, 441 U.S. at 452–53. The Court stated: "Under this Convention, containers temporarily imported are admitted free of 'all duties and taxes whatsoever chargeable by reason of importation.' 20 U.S.T. at 304. The Convention reflects a national policy to remove impediments to the use of containers as 'instruments of international traffic.' 19 U.S.C. § 1322 (a)."

61. *Japan Line*, 441 U.S. at 453.

62. The Court in *Japan Line* feared the "acute" risk of retaliatory taxes by Japan, which "of necessity would be felt by the Nation as a whole." *Id.* The Court also pointed out that retaliation by some nations could be automatic (*e.g.*, West German law provides for a reciprocal response to taxes on its instrumentalities of commerce). *Id.* n.18. See Brief for Appellants, 19–20, *Japan Line*, 441 U.S. 434, noting that at least eight foreign governments have expressed concern to the State Department because the California tax was imposed.

containers is desirable in some contexts[63] does not render it necessary or even desirable in all contexts.

Neither should the risk of retaliatory taxes have dictated the Court's interpretation of the commerce clause. International tax apportionment could have been arranged by treaty.[64] It is dubious that the harm of retaliatory taxes[65] is any greater than that of denying a state its right to charge for services rendered on an apportioned nondiscriminatory basis. And although different states might tax containers at different rates,[66] their taxes could vary only in relation to the containers' actual presence in the taxing jurisdiction and the character of the services rendered by the ports.[67]

The Court adopted the phrase "speaking with one voice" from *Michelin Tire Corp. v. Wages*[68] without embracing either its reasoning or conclusion. The underlying issue in *Michelin Tire* is identical to the issue in *Japan Line*;[69] the policies animating both the import-export clause and the commerce clause are "much the same."[70] Yet, in *Michelin* the Court concluded that such "nondiscriminatory property taxation can have no impact whatsoever on the Federal Government's exclusive regulation of foreign commerce, [because] . . . it cannot be applied selectively to encourage or discourage any importation in a manner inconsistent with federal regulation."[71] By the same reasoning, an apportioned nondiscriminatory property tax does not interfere with the federal government's right to regulate foreign commerce under the commerce clause.[72] The Court in *Michelin* stressed that "only the clearest constitutional mandate should

63. For example, the Customs Convention on Containers, art. I(b), May 18, 1956, [1969] 20 U.S.T. 301, 304, T.I.A.S. No. 6634, grants containers " 'temporary admission free of import duties and import taxes and free import prohibitions and restrictions,' provided they are used solely in foreign commerce and are subject to re-exportation. 20 U.S.T. at 304." *See Japan Line*, 441 U.S. at 446 n.10.

64. *See, e.g.*, Clark, *Property Taxation of Foreign Goods & Enterprises—A Study in Inconsistency*, 4 PEPPERDINE L. REV. 39, 59 (1976); Amicus Brief of the MultiState Tax Commission and Participating States at 42, *Japan Line*, 441 U.S. 434.

65. The Court sought to avoid the levy of such taxes by foreign nations. *Japan Line*, 441 U.S. at 453.

66. *See, e.g.*, *Japan Line*, 441 U.S. at 453.

67. This idea is illustrated by the implication in *Michelin Tire*, 423 U.S. 276, 287, that foreign commerce should be taxed on a par with interstate commerce.

68. 423 U.S. 276 (1976).

69. The underlying issue in both cases is whether a state may impose reasonable taxes to finance services rendered, when all goods are assessed equally on the basis of actual presence.

70. 441 U.S. at 449 n.14. One of the principal purposes of the import-export clause, which prohibits state imposts or duties on imports, is to vest in the federal government the exclusive power to regulate foreign commerce. *Michelin Tire*, 423 U.S. at 285–86. The commerce clause similarly secured for the federal government the exclusive power to regulate foreign commerce. *See Japan Line*, 441 U.S. at 449–50 n.14; *Michelin Tire*, 423 U.S. at 290 n.11.

71. 423 U.S. at 286.

72. The federal government is free to preempt the field at any time.

lead us to condemn such taxation.''[73] The existence of such a constitutional mandate in *Japan Line* is far from clear.

C. *Implications of* Japan Line

By making it unconstitutional for states to tax foreign instrumentalities of commerce, the decision in *Japan Line* revives the expressly overruled principle of *Spector Motor Service, Inc. v. O'Connor,*[74] that certain segments of commerce enjoy constitutional immunity from state taxation.[75] The *Japan Line* Court's interpretation of the commerce clause not only harms the states' interests but places the United States at a disadvantage in international commerce. If Japan or another nation begins taxing instrumentalities of foreign commerce, the states will be constitutionally barred from responding with a like tax, and Congress, unlike other national governments, cannot levy a direct property tax.[76] Denying such taxes to the states places the United States in an awkward situation if the

73. 423 U.S. at 293.

74. Spector Motor Serv., Inc. v. O'Connor, 340 U.S. 602 (1951), was expressly overruled in Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 288–89 (1977). The Court in *Complete Auto Transit,* 430 U.S. at 287, quoting from Colonial Pipeline Co. v. Traigle, 421 U.S. 100, 108 (1975), stated:

> [D]ecisions of this Court, particularly during recent decades, have sustained nondiscriminatory, properly apportioned state corporate taxes upon foreign corporations doing an exclusively interstate business when the tax is related to a corporation's local activities and the State has provided benefits and protections for those activities for which it is justified in asking a fair and reasonable return.

In *Colonial* the Court sustained a Louisiana franchise tax that had been carefully reworded from a tax on the privilege of "carrying on or doing business" in the State to one upon "the qualification to do business in this State or the actual doing of business within this State in a corporate form." According to the evidence before the Court in *Complete Auto Transit,* the tax was apportioned, nondiscriminatory, and sufficiently related to benefits provided by the State. This decision effectively stripped *Spector Motor* of any force by distinguishing it only on the grounds that *Spector Motor* involved a tax on the privilege of carrying on interstate commerce.

75. The rule of *Spector Motor* had its origin in Freeman v. Hewit, 329 U.S. 249 (1946), in which Mr. Justice Frankfurter stated that interstate commerce should enjoy a sort of "free trade" immunity from state taxation. The Court in *Spector* relied upon this analysis to strike down a Connecticut "tax or excise upon [a Missouri corporation's] franchise for the privilege of doing business within the State" measured by apportioned net income. The *Spector* rule was gradually whittled down until expressly overruled in *Complete Auto Transit,* where the Court upheld the constitutionality of a tax on the "privilege of doing business" in Mississippi. The Court, quoting from *Colonial,* stated:

> It is a truism that the mere act of carrying on business in interstate commerce does not exempt a corporation from state taxation. 'It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business.' *Western Live Stock v. Bureau of Revenue,* 303 U.S. 250, 254 (1938). *Colonial Pipeline Co. v. Traigle,* 421 U.S. at 108.

430 U.S. at 288.

76. U.S. CONST. art. I, § 2, cl. 3 and art. I, § 9, cl. 4 require that "direct" taxes be apportioned among the several states in accordance with their respective populations. J. FREELAND, S. LIND, R. STEPHENS, FUNDAMENTALS OF FEDERAL INCOME TAXATION: CASES AND MATERIALS 14 (2d ed. 1977).

present system of international tax forebearance should change. The federal government's only alternatives would be either to levy a federal excise tax or to attempt to negotiate a treaty precluding taxation of instrumentalities of foreign commerce. The United States' bargaining position is weakened, however, if neither a state nor the federal government has constitutional authority to assess ad valorem taxes.

Furthermore, the exemption of foreign commercial instrumentalities from taxes otherwise imposed on goods in interstate commerce may itself constitute impermissible discrimination. Although the United States Supreme Court has yet to consider favoring international over domestic commerce, it has been quick to strike down any tax favoring local over interstate commerce.[77] By analogy, it should condemn taxes which discriminate against domestic commerce in favor of foreign commerce.[78] Many commentators agree that the federal system should require states to accord "neutral" treatment to interstate and foreign commerce.[79] The nondiscriminatory tax invalidated in *Japan Line* should have been upheld on this basis.

The Court has voiced loud concern for "uniformity" without considering the best means to promote it.[80] As recently as 1978, the Court conceded that Congress should decide such issues. Congressional authority under the commerce clause would justify the enactment of legislation dictating uniform rules. Indeed, the Court admitted that "[i]t is to that body

77. *See* note 18 *supra*.

78. In Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318 (1977), the Court indicated generally that taxes favoring one class of regulated commerce over another are prohibited. Relying upon *Boston Stock Exchange*, the California court of appeal recently invalidated a tax that discriminated in favor of foreign commerce. Zee Toys, Inc. v. County of Los Angeles; Sears, Roebuck and Co. v. County of Los Angeles, 85 Cal. App. 3d 763, 149 Cal. Rptr. 750 (1978)(striking down an ad valorem tax levied upon tangible personal property in plaintiffs' possession, stored in warehouses in Los Angeles County on the tax lien dates, because the tax was not imposed on foreign goods and the tax afforded foreign goods a competitive advantage over interstate goods, which was deemed to be a regulation of interstate and foreign commerce in violation of the commerce clause) (consolidated cases). The United States Supreme Court has heard *Sears, Roebuck* on appeal. 48 U.S.L.W. 3459 (January 22, 1980). The case has been restored to the calendar for reargument. 48 U.S.L.W. 3698 (April 29, 1980).

79. *See, e.g.*, Clark, *Property Taxation of Foreign Goods & Enterprises—A Study in Inconsistency*, 4 PEPPERDINE L. REV. 39, 79 (1976); Comment, *State Taxation of International Air Carriers*, 57 NW. U. L. REV. 92, 103 (1962). *See also* Sea-Land Serv., 117 Cal.2d 447, 528 P.2d 56, 67 (1974). *But see* Miller, *Foreign Commerce and State Power: The Constitutionality of State Buy American Statutes*, 12 CORNELL INT'L. L.J. 109 (1979) ("a proposal to revitalize the foreign commerce clause"); Comment, *Limitations On State Taxation of Foreign Commerce: The Contemporary Vitality of the Home-Port Doctrine*, 127 U. PENN. L. REV. 817 (1979) (although "anachronistic," the home port doctrine is "most prudent"); Note, *Alternative Theories for Establishing a Federal Common Law of Foreign Judgments in Commerical Cases: The Foreign Affairs Power and the Dormant Foreign Commerce Clause*, 16 VA. J. INT'L. L. 635, 658 (1976).

80. *See* Section III *infra*.

and not this Court, that the Constitution has committed such policy decisions."[81] Other commentators share this position.[82] Nevertheless, in *Japan Line* the Court dictated United States international tax policy.

IV. ALTERNATIVES

The possibility of entering into an international tax treaty offers one solution to the problem of double taxation.[83] The United States is party to several international agreements affecting instrumentalities of commerce.[84] Containers could be exempted from ad valorem property taxation by such a convention or treaty.[85] One obstacle to such an international agreement is Congress' understandable reluctance to interfere with

81. In Moorman Mfg. Co. v. Bair, 437 U.S. 267, 280 (1978), the Court explained:

> While the freedom of the States to formulate independent policy in this area may have to yield to an overriding national interest in uniformity, the content of any uniform rules to which they must subscribe should be determined only after due consideration is given to the interests of all affected States. It is clear that the legislative power granted to Congress by the Commerce Clause of the Constitution would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income. It is to that body and not this Court, that the Constitution has committed such policy decisions.

82. The Court has attempted to construct a consistent national program of international taxation on a case by case basis. It should have left tax policy to be developed by experts in national and international taxation. *See* Hellerstein, *State Taxation Under the Commerce Clause: An Historical Perspective*, 29 VAND. L. REV. 335, 350–51 (1976); Note, *State Taxation of Foreign Aircraft Used In Foreign Commerce*, 49 CALIF. L. REV. 968, 973–74 (1961).

83. *See, e.g., Japan Line*, 441 U.S. at 454–55; *Scandinavian Airlines Sys.*, 56 Cal. 2d 11, 14 Cal. Rptr. at 48, 363 P.2d at 48 (Traynor, J. dissenting); Note, *State Taxation of Foreign Aircraft Use in Foreign Commerce*, 49 CALIF. L. REV. 968, 974 (1961); Comment, *State Taxation of International Air Transport*, 11 STAN. L. REV. 518, 536–37 (1959). Even after *Japan Line*, assuming that the United States could negotiate a tax treaty (*see* text following note 75 *supra*) a tax treaty could prevent foreign nations from taxing in a way that our nation is no longer constitutionally able to do.

84. *E.g.*, Customs Convention of Containers, May 18, 1956, [1969] 20 U.S.T. 301, T.I.A.S. No. 6634, 338 U.N.T.S. 103; Interim Agreement on International Civil Aviation, Dec. 7, 1944, 59 Stat. 1516, E.A.S. No. 469, 15 U.N.T.S. 205 (International Civil Aviation Organization Council Resolution III, November 1966). *See* Comment, *Limitations on State Taxation of Foreign Commerce: The Contemporary Vitality of the Home-Port Doctrine*, 127 U. PENN. L. REV. 817, 835 (1979). For a list of the numerous bilateral and multilateral conventions to which Japan adheres, see A. EHRENSWEIG, S. IKEHARA, N. JENSEN, BILATERAL STUDIES IN PRIVATE INTERNATIONAL LAW—NO. 12: AMERICAN-JAPANESE PRIVATE INTERNATIONAL LAW 24, 137–46 (1964).

85. For example, the OECD model double taxation convention of income and on capital suggests a simple rule based on a single taxing authority. ORGANIZATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, MODEL DOUBLE TAXATION CONVENTION ON INCOME AND ON CAPITAL (1977). In Chapter IV—Taxation of Capital, Article 22—Capital, the OECD recommends:

> Capital represented by ships and aircraft operated in international traffic and by boats engaged in inland waterways transport, any by movable property pertaining to the operation of such ships, aircraft and boats, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

Id. at 38. *See also* Commentary on Article 22; *id.* at 143.

state taxing power.[86] As a result of the Court's decision, however, the odds of successfully negotiating such a treaty are diminished.[87]

A more realistic alternative is congressional regulation. If, before *Japan Line*, Congress had decided that a state tax upon instrumentalities of international commerce unduly interfered with the nation's foreign relations, it could have exercised its commerce power, precluding such taxation by statute. At the same time Congress might have found alternative means of recompensing states that provide services to international containers. The result in *Japan Line*, however, constitutionally restricts the states' legitimate taxing power and is thus less flexible and retractable than congressional preemption. The result should serve as an invitation to Congress to consider whether overriding legislation is possible.[88]

V. CONCLUSION

By deferring largely to the interests of foreign taxing authorities, the Court has severely impaired the states' ability to obtain compensation for services they provide. Its rule of constitutional construction rejects a rea-

86. The Senate approved a version of the United States-United Kingdom income tax treaty on June 27, 1978. In that version the Senate reserved as to Article 9(4), which prohibited any state from using the unitary apportionment system to determine its share of taxable income of U.K. enterprises and subsidiaries. Under the unitary concept a state seeks a portion of a multi-state or multi-national company's consolidated income on the basis of a predetermined formula. The California formula requires foreign-owned corporations to provide sales and wage information about all their worldwide operations, not merely those in California. The U.K., the Netherlands, Canada, and Japan complained about the unusually broad disclosure required by the state of California. Nonetheless, the final version of the treaty, approved by the Senate on July 9, 1979, contains no prohibition on the use of the unitary apportionment system. Articles of ratification were exchanged on March 25, 1980, and the treaty entered into force on April 25, 1980. [1980] TAX TREATIES II (P-H) ¶ 89,001. *See* Burge, *The United States-United Kingdom Income Tax Treaty*, in INCOME TAX TREATIES 683, 700–01 (J. Bischel ed. 1978).

87. *See* text following note 75 *supra*.

88. *See* Kaplan, *United States: Taxing Foreign Firms by Formula*, TAX MANAGEMENT INT'L. J., (September 1979), at 3: "[I]t is possible that Congress will accede to pressure from the states to reverse the holding of the *Japan Line* case by federal statute." *Id.* at 19. Congress might be able to find a way to compensate the states for the services they provide to instrumentalities in international commerce, for example through revenue sharing. *See* Note, *State Taxation of Foreign Commerce*, 45 J. AIR L. & COMMERCE 559, 573 (1980). Alternatively, Congress may be able to override a constitutional holding by the Supreme Court. Congress has twice previously enacted legislation indicating that interstate commerce may be subject to certain state regulation though the Supreme Court had invalidated it under the commerce clause. *See, e.g.*, the Wilson Act, 26 Stat. 313 (1890), enabling states to prohibit sale in the original package of liquor brought from other states. The Supreme Court had previously struck down such legislation in Leisy v. Hardin, 135 U.S. 100, 109–10 (1890). The Court sustained the constitutionality of the Wilson Act in *In re* Rahrer, 140 U.S. 545 (1891). Congress similarly overrode the Court's restriction of states' power in Bowman v. Chicago & Northwestern Ry. Co., 125 U.S. 465 (1888). The Webb-Kenyon Act, 37 Stat. 699–700 (1913), allowed a state to prohibit the importation of liquor. Bikle, *The Silence of Congress*, 41 HARV. L. REV. 200, 203–07 (1927). Congress would be best informed as to what precise alternative solutions are available.

sonably apportioned nondiscriminatory tax in favor of maintaining symmetry in the current international tax structure which may be transitory at best.[89] Abruptly the Court has abandoned its own constitutional rules developed over many years. Its judgment on national tax policy is essentially a legislative one, not compelled by any constitutional principle recognized in the past. Congress should intervene to develop rules under which instrumentalities in foreign commerce, as in interstate commerce, may properly be subjected to nondiscriminatory state taxes, assessed on a reasonably apportioned basis.

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89. *E.g.*, the West German taxing system would change automatically if another nation began to tax instrumentalities of international commerce. *Japan Line*, 441 U.S. at 453 n.18. *See* Clark, *Property Taxation of Foreign Goods and Enterprises—A Study In Inconsistency*, 4 PEPPERDINE L. REV. 39, 79 (1976). The Court in *Japan Line* stressed that the California tax created multiple taxation in fact. *Japan Line*, 441 U.S. at 452.