In The

Supreme Court of the United States

HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent.

On Petition For A Writ Of Certiorari To The Texas Court Of Appeals, Sixth Appellate District

PETITION FOR A WRIT OF CERTIORARI

DOUGLAS W. ALEXANDER
Counsel of Record
AMY WARR
ALEXANDER DUBOSE & TOWNSEND LLP
515 Congress Avenue
Suite 2350
Austin, Texas 78701
(512) 482-9300
dalexander@adtappellate.com

ROGER TOWNSEND
ALEXANDER DUBOSE & TOWNSEND LLP
1844 Harvard Street
Houston, Texas 77008
(713) 523-2358

ROY T. ENGLERT, JR.
ROBBINS, RUSSELL, ENGLERT, ORSECK, UNTEREINER & SAUBER LLP
1801 K Street, N.W.
Suite 411
Washington, D.C. 20006
(202) 775-4500

KIRK SWINNEY
MCCREARY, VESELKA, BRAGG & ALLEN, P.C.
700 Jeffrey Way, Suite 100
Round Rock, Texas 78665
(512) 323-3200

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

Blank Page

QUESTION PRESENTED

Whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport.

TABLE OF CONTENTS

TABLE OF CONTENTS – Continued

TABLE OF CONTENTS – Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES – Continued

TABLE OF AUTHORITIES – Continued

Blank Page

PETITION FOR A WRIT OF CERTIORARI

The Texas court of appeals held a generally applicable, nondiscriminatory state ad valorem tax to be unconstitutional, as applied to natural gas in storage on an interstate pipeline system. App., *infra*, 22. On virtually identical facts the Supreme Court of Oklahoma, "unpersuaded by [the Texas] court's reasoning," held such a tax to be constitutional. *In re Assessment of Personal Prop. Taxes Against Mo. Gas Energy*, 234 P.3d 938, 959 n.84 (Okla. 2008), *cert. denied*, 130 S. Ct. 1685 (2010). Before denying certiorari in *Missouri Gas*, this Court invited the Solicitor General to express the views of the United States. The Solicitor General advised the Court that the Oklahoma Supreme Court had reached the right result on the constitutional merits and the conflicting decision of the Texas court was therefore wrong:

> The Oklahoma Supreme Court correctly held that, under this Court's modern dormant Commerce Clause jurisprudence, petitioner had failed to establish the unconstitutionality of applying the State's ad valorem tax on personal property to stored natural gas.

Br. for U.S. (No. 08-1458), at 9.

Now that the Texas court's decision is final, this Court should grant certiorari, resolve the conflict between the decision below and the decision of the Supreme Court of Oklahoma, and reach the same conclusion on the merits that the Solicitor General did in *Missouri Gas*.

OPINIONS BELOW

The opinion of the state court of appeals (App., *infra*, 1-22) is reported at *Peoples Gas, Light, and Coke Co. v. Harrison Cent. Appraisal Dist.*, 270 S.W.3d 208 (Tex. App. – Texarkana 2008, pet. denied). The state trial court issued findings of fact and conclusions of law (App., *infra*, 25-45), which are unreported.

JURISDICTION

The judgment of the Texas Sixth District Court of Appeals (App., *infra*, 23-24) was entered on September 24, 2008. The Supreme Court of Texas denied review of that judgment on March 12, 2010 (App., *infra*, 48), and denied rehearing on October 1, 2010 (App., *infra*, 49). The jurisdiction of this Court rests on 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause provides: "The Congress shall have power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. Const., Art. I, § 8, cl. 3.

Section 11.01 of the Texas Tax Code provides:

> (a) All real and tangible personal property that this state has jurisdiction to tax is taxable unless exempt by law.
>
> (b) This state has jurisdiction to tax real property if located in this state.
>
> (c) This state has jurisdiction to tax tangible personal property if the property is:
>
> > (1) located in this state for longer than a temporary period;
> >
> > (2) temporarily located outside this state and the owner resides in this state; or
> >
> > (3) used continually, whether regularly or irregularly, in this state.
>
> (d) Tangible personal property that is operated or located exclusively outside this state during the year preceding the tax year and on January 1 of the tax year is not taxable in this state.

Tex. Tax Code § 11.01.

STATEMENT

Like the *Missouri Gas* case, "[t]his case involves a State's taxation of natural gas stored in underground facilities located in the State and connected to a pipeline system for interstate transport." Br. for U.S.

(No. 08-1458), at 1. The narrow constitutional question presented in both cases is the same: whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport.

There is no material difference between this case and *Missouri Gas*. Yet the Texas and Oklahoma courts employed differing analyses and therefore reached conflicting results in resolving the same constitutional question. The explanation for this confusion is that gaps remain in this Court's modern dormant Commerce Clause jurisprudence. This case affords the Court the opportunity to resolve the direct conflict between Texas and Oklahoma, and also address a broader set of continuing constitutional controversies that are of immense practical and jurisprudential importance.

A. Factual Background

The Solicitor General recited the underlying facts of the *Missouri Gas* case in her invited amicus brief. *See* Br. for U.S. (No. 08-1458), at 1-4. Those facts are materially indistinguishable from the facts of this case.

Respondent The Peoples Gas, Light and Coke Company (Peoples) is a natural gas distribution company that purchases gas from shippers on a FERC-regulated interstate natural gas pipeline

system operated by Natural Gas Pipeline Company of America (Pipeline).[1] RR 2:63, 66-67, 69, 77. Peoples ultimately sells the gas to consumers in Chicago. RR 2:63.

As part of its system, Pipeline operates a large underground storage facility in North Lansing, Harrison County, Texas, one of several Pipeline storage facilities. RR 2:30, 72, 169. A storage facility is not part of the interstate pipeline; it is a facility connected to the pipeline. *Id.* Pipeline's storage facilities allow customers such as respondent Peoples to purchase natural gas during the summer (when demand is low and the gas is less expensive) and have it stored until delivery to consumers during the winter (when demand is high and the gas is more expensive). RR 2:32-33, 73, 105-06; 4:48. To put natural gas into the underground storage facility, one must remove it from the pipeline and inject it with compressors. RR 3:13-14.

In conformity with the mandate of the Texas Constitution that "[a]ll real property and tangible personal property in this State . . . shall be taxed in proportion to its value," Tex. Const., Art. VIII, § 1(b), the Texas Tax Code authorizes ad valorem taxation of

---

[1] Because this case was tried in Texas, the record appears in two distinct formats. The Reporter's Record (cited as "RR [volume]:[page]") consists of the transcript of the trial court proceedings and trial exhibits. The Clerk's Record (cited as "CR [volume]:[page]") consists of the pleadings, orders, and other documents filed in the case. "PX" stands for "Plaintiff's Exhibit."

real and tangible personal property in the State. Tex. Tax Code § 11.01(a). Section 11.01(a) does not discriminate between goods in intrastate and interstate commerce, but applies generally to all non-exempt goods that the State has jurisdiction to tax. *Id.*

Pursuant to § 11.01(a), Pipeline pays ad valorem taxes to local taxing authorities on its so-called *cushion gas* in North Lansing. RR 2:29-30, 174; 4:17. Cushion gas must remain in the storage facility to provide the necessary pressure so that *working gas* may be delivered to the pipeline. *Id.* Working gas is the balance of the gas in the storage facility that is ultimately removed from storage for transport and delivery to consumers. *Id.*

Pipeline never takes title to working gas while that gas is in the pipeline system. RR 2:175. Pipeline's customers (including Peoples) own the volumes of working gas on the system. RR 2:174; 4:27. If a storage customer "nominates" a volume of gas to be delivered out of its storage account, Pipeline delivers it pursuant to contract. RR 2:175.

For tax years 2003-2005, petitioner Harrison Central Appraisal District included on the tax rolls Peoples' allocable share (as well as the allocable shares of other owners) of the working gas balance of the natural gas stored at North Lansing. RR 3:28, 154-55, 159; PX 1, 4, 7. The allocation was based on Pipeline's records. RR 3:155. Those records included invoices showing the quantity of gas that Peoples had

in storage with Pipeline, systemwide, during the years in question. RR 2:104.

B. Proceedings Below

Peoples protested the Appraisal District's assessments of its working gas. PX 2, 5, 8. After a bench trial, a state trial court entered a judgment that the Appraisal District has the authority to assess the working gas. App., *infra*, 44-45, 46.

The Texas Sixth District Court of Appeals reversed that judgment. App., *infra,* 23. The court rejected Peoples' argument that it did not own the volumes of gas allocated to it for tax purposes. *Id.*, at 5-9. But the court accepted Peoples' argument that the Commerce Clause shields Peoples' gas from state taxation. *Id.*, at 10-22.

One month later, the Supreme Court of Oklahoma issued a contrary decision on materially indistinguishable facts and stated that it was "unpersuaded by [the Texas] court's reasoning." *Missouri Gas,* 234 P.3d, at 959 n.84.

The Supreme Court of Texas denied discretionary review of the decision below. That denial presents this Court with a direct conflict on an important, recurring question of constitutional law between a reviewable decision, which the highest court of Texas has declined to disturb, and a decision of the highest court of Oklahoma.

REASONS FOR GRANTING THE PETITION

This Court should grant the petition to resolve the conflicting responses of Texas and Oklahoma courts to the same constitutional question. The Texas court below held that the Commerce Clause *prohibits* state ad valorem taxation of natural gas in storage on an interstate pipeline system. App., *infra*, 22. The Supreme Court of Oklahoma held that the Commerce Clause *permits* such a tax. *Missouri Gas*, 234 P.3d, at 959 n.84. That conflict means that natural gas on an interstate pipeline system is taxable by state authorities if it is in storage in Oklahoma, but not if it is in storage in neighboring Texas.

The Texas and Oklahoma courts reached those conflicting results because they employed differing constitutional analyses. They did so because, in the context of state ad valorem taxation of goods in interstate commerce, it remains unclear whether or to what extent the four-pronged test this Court adopted in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), is affected by other, older aspects of this Court's Commerce Clause jurisprudence.

"The Commerce Clause is an express grant of power to Congress to 'regulate Commerce . . . among the several States.'" *United States v. Int'l Bus. Machines Corp.*, 517 U.S. 843, 852 n.2 (1996) (citing U.S. Const., Art. I, § 8, cl. 3). "It does not expressly prohibit the States from doing anything. . . ." *Id.* Yet this Court has long held that "the Commerce Clause is more than an affirmative grant of power; it has a

negative sweep as well." *Quill Corp. v. North Dakota*, 504 U.S. 298, 309 (1992) (citing *Gibbons v. Ogden,* 22 U.S. (9 Wheat.) 1, 231-32, 239 (1824) (Johnson, J., concurring)). This so-called "negative" or "dormant" Commerce Clause, *id.*, "limits the power of the States to erect barriers against interstate trade." *Lewis v. BT Inv. Managers, Inc.*, 447 U.S. 27, 35 (1980).

This Court's interpretation of the dormant Commerce Clause "has evolved substantially over the years, particularly as that Clause concerns limitations on state taxation powers." *Quill*, 504 U.S., at 309. In 1977, the Court issued its watershed decision in *Complete Auto,* 430 U.S., at 274. The Court noted that in prior cases it had already "rejected the proposition that interstate commerce is immune from state taxation." *Id.*, at 288. Because "'[i]t 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,'" *id.*, at 279 (quoting *Western Live Stock v. Bureau of Revenue,* 303 U.S. 250, 254 (1938)), the Court adopted a new, four-pronged test for state taxes on those engaged in interstate commerce. A state tax survives a Commerce Clause challenge if it "[1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State." *Id.*

Although that four-pronged test has provided a greater measure of predictability to modern dormant

Commerce Clause analysis, unanswered questions remain. First, as the Solicitor General observed, there remains a question regarding the continuing applicability of the Court's "continuity of transit" cases such as *Minnesota v. Blasius*, 290 U.S. 1, 9-12 (1933):

> This Court has not yet decided whether or to what extent *Complete Auto* displaces the older line of "continuity of transit" cases in the specific context of state ad valorem taxes on goods temporarily held in storage during the course of interstate transport.

Br. for U.S. (No. 08-1458) at 10. Second, there remains a question as to whether a "physical-presence" rule, which the Court has held remains applicable in analyzing Commerce Clause challenges to state *sales* and *use* taxation, *Quill*, 504 U.S., at 312-14, likewise applies to ad valorem *property* taxation.

The Supreme Court of Oklahoma in *Missouri Gas* held that both aspects of this Court's older cases were inapplicable. The Texas court below, by contrast, held that they were crucial to the analysis. Those courts' conflicting interpretations of this Court's jurisprudence resulted in their conflicting answers to the same constitutional question.

This Court should grant the petition because, as demonstrated below, the narrow constitutional question presented and the two broader constitutional controversies out of which that question arises are of immense practical and jurisprudential importance, and they are recurring. Moreover, the

decision below is erroneous. The Solicitor General so concluded when she determined that the Oklahoma court, not the Texas court, correctly resolved the constitutional issue presented. *See* Br. for U.S. (No. 08-1458), at 9. This Court should reach the same result here.

I. The Constitutional Question Presented is Important to State Taxing Authorities and Industry Participants Alike.

A. Whether Natural Gas in Storage on an Interstate Pipeline is Immune from State Taxation is Important and Recurring.

The narrow constitutional question presented in this case is the same as the question presented in *Missouri Gas*: whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport. That this question is important is evident from this Court's invitation to the Solicitor General in *Missouri Gas* to express the views of the United States on the question. *See* Br. for U.S. (No. 08-1458), at 1. That the Solicitor General ultimately concluded that the Supreme Court of Oklahoma reached the right result for the right reasons underscores why the conflicting decision by the Texas court in this case should be reversed.

Not only is the constitutionality of subjecting natural gas in storage to state property taxation important to this Court's dormant Commerce Clause jurisprudence, but the Court's answer will have enormous practical consequences. According to the American Petroleum Institute, natural gas is a $385 billion industry in this country.[2] FERC-regulated interstate natural gas pipelines move nearly a quarter of the nation's energy long distances to markets in the 48 contiguous states.[3] Storage of natural gas on the interstate pipeline system is an important and integral feature of the system. At the close of 2007, 400 underground natural gas storage sites were operational in the United States.[4]

Storage affords great benefit to shippers. It allows them to practice price arbitrage by purchasing natural gas during the summer (when demand is low and the gas is less expensive) and having it stored until delivery to consumers during the winter (when demand is high and the gas is more expensive). RR 2:32-33, 73, 105-06; 4:48.

---

[2] Am. Petroleum Inst., *Natural Gas Is America's New Frontier* 1 (2010), http://www.api.org/aboutoilgas/NATGAS_111610.pdf.

[3] Fed. Energy Regulatory Comm'n, *An Interstate Natural Gas Facility on My Land? What Do I Need to Know?* 2 (2010), http://ferc.gov/for-citizens/citizen-guides/citz-guide-gas.pdf.

[4] U.S. Energy Information Admin., Independent Statistics and Analysis, About U.S. Natural Gas Pipelines, Underground Natural Gas Storage, Underground Storage by U.S. Region, http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrnd_storage.html (last visited Dec. 27, 2010).

The sheer volumes involved are tremendous. The single pipeline company involved in this case has approximately 250 *billion* cubic feet of storage available systemwide. RR 2:163. Thus, whether natural gas in storage on an interstate pipeline system is subject to state property taxation (as the Supreme Court of Oklahoma held and the Solicitor General agreed), or is constitutionally immune from such taxation (as the Texas court held), is of considerable practical importance both to industry participants (which can at least pass along costs to their ratepayers) and to cash-strapped state and local governments.

The recurring nature of this constitutional issue is evident from its coming before this Court twice within a short period of time – first in *Missouri Gas* and then in this case. The nature of the conflicting decisions virtually ensures that the issue will further recur. Any State that has a natural gas storage facility will be encouraged by the Oklahoma decision to tax the working gas stored in that facility. Any taxpayer that faces such taxation will be encouraged by the Texas decision to contest the tax. No state court will be confident as to which analysis is correct unless and until this Court addresses it.

Industry participants have recognized that the issue is recurring and should be addressed by this Court. In its amicus brief to this Court in the *Missouri Gas* case, the American Gas Association stated: "The *ad valorem* taxation of natural gas in FERC-regulated storage within the interstate transportation system presents a recurring issue that merits this Court's attention." AGA Amicus Br. (No.

08-1458), at 3. Because all agree that this constitutional issue is important and recurring, the Court should grant the petition to resolve the conflicting decisions.

B. The Broader – and Also Recurring – Constitutional Questions Make this Case Even More Important.

The substantial importance of the narrow constitutional question presented is amplified by the constitutional controversies out of which that question arises: (1) whether or to what extent this Court's "continuity of transit" analysis applies to modern dormant Commerce Clause analysis after *Complete Auto*; and (2) whether the "physical-presence" requirement, which the Court reaffirmed in *Quill* as to *sales* and *use* taxation, likewise applies to ad valorem *property* taxation. The Court's answers to those questions will affect a far broader range of goods than natural gas.

1. The "Continuity of Transit" Issue is Important and Recurring.

As the Solicitor General explained in *Missouri Gas*, there are "two different lines of dormant Commerce Clause precedents." Br. for U.S. (No. 08-1458), at 9. "In its earlier cases, dating back to the late nineteenth century, this Court applied a 'continuity of transit' analysis to determine whether goods being transported through a State could be subjected to state property taxes." *Id.* "Under that approach, the critical question was whether the interstate transit of

goods had been sufficiently interrupted for purposes other than merely facilitating the transit; if so, the goods were deemed locally taxable." *Id.*, at 9-10.

"In *Complete Auto* this Court announced a new general framework for resolving dormant Commerce Clause challenges to state taxes." *Id.*, at 10. "The Court held that a state tax will be sustained against a dormant Commerce Clause challenge if it [satisfies the Court's four-pronged test]." *Id.* "The Court also overruled its prior holdings that any tax on the 'privilege of doing [interstate] business' was unconstitutional per se." *Id.* (citing *Complete Auto*, 430 U.S., at 288-89). "As compared to the Court's prior 'continuity of transit' decisions, the *Complete Auto* framework requires a more comprehensive inquiry, consistent with the Court's rejection of the per se rule against state taxation of interstate commerce." *Id.*

The Texas court of appeals in this case focused heavily on this Court's "continuity of transit" line of authorities, citing a whole string of pre-*Complete Auto* decisions.[5] Based on those authorities, the court concluded that "[t]he crucial question in determining whether the state may exert its taxing power is

---

[5] *See* App., *infra*, 11-14, 17 (citing *Coe v. Errol*, 116 U.S. 517, 527 (1886); *Hughes Bros. Timber Co. v. Minnesota*, 272 U.S. 469, 476 (1926); *Indep. Warehouses v. Scheele*, 331 U.S. 70, 73 (1947); *Carson Petroleum Co. v. Vial*, 279 U.S. 95, 101 (1929); *Blasius*, 290 U.S., at 9-10; *Champlain Realty Co. v. Town of Brattleboro*, 260 U.S. 366, 377 (1922); and *Mich.-Wis. Pipe Line Co. v. Calvert*, 347 U.S. 157, 166-68 (1954)).

whether there is 'continuity of transit.'" App., *infra*, 13. The Texas court then concluded that "[t]he natural gas allocated to Peoples is in the stream of interstate commerce, and this storage does not remove it from interstate commerce." *Id.*, at 17.

Having made the threshold determination that the gas allocated to Peoples was in "continuity of transit," the court, in its ensuing *Complete Auto* analysis, attached little significance to the fact that large volumes of the gas were continuously present in Harrison County, Texas. The court also found it compelling that Pipeline, not Peoples, decided where the gas was to be stored. App., *infra*, 19-20. Under that analysis, the court held the connection between the State of Texas and Peoples' large inventories of storage gas in Texas to be "too tenuous to subject Peoples to ad valorem taxation in Texas." *Id.*, at 20.

In direct conflict with that approach, the Supreme Court of Oklahoma rejected the Texas court's reliance on the "traditional continuity of transit analysis" because it was "superseded by the Supreme Court's decision in *Complete Auto Transit v. Brady*." *Missouri Gas*, 234 P.3d, at 959 n.84. The Court also rejected as immaterial to the *Complete Auto* analysis the factor that the Texas court found to be compelling – that Pipeline, not Peoples, was "the decision maker with respect to the place of storage. . . ." *Id.*

As noted above, the Solicitor General observed that this Court has yet to decide whether or to what extent the "continuity of transit" analysis retains

vitality in Commerce Clause analysis. Br. for U.S. (No. 08-1458), at 10. The Supreme Court of Oklahoma noted the same dearth of authority: "While the [U.S. Supreme] Court has applied the [*Complete Auto*] test to many kinds of taxes, it has never addressed whether the [*Complete Auto*] test applies to an ad valorem tax on goods in the process of being transported in interstate commerce." *Missouri Gas*, 234 P.3d, at 953 (citing *Complete Auto*, 430 U.S. at 279).

A leading tax commentator has likewise noted this lack of clarity. Although "[s]ome of the results of the doctrinal changes" brought about by this Court in recent years "are clear," "the impact of the contemporary Commerce Clause philosophy on other cases decided in earlier eras, and the doctrine they spawned, is less clear." 1 J. Hellerstein & W. Hellerstein, State Taxation ¶ 4.13[1] (3d ed. 2010).

The continuing uncertainty about the role, if any, of "continuity of transit" implicates the full range of goods that taxpayers might argue are in the course of interstate transport. A recent example is a decision holding that oil in a tank farm is immune from state property taxation. *See Midland Cent. Appraisal Dist. v. BP Am. Production Co.*, 282 S.W.3d 215, 224 (Tex. App. – Eastland 2010, pet. denied). Relying on this Court's pre-*Complete Auto* jurisprudence, and citing the decision below, the *Midland Central* court held that because the oil was "in transit in the stream of interstate commerce," state property taxation of the oil was prohibited by the Commerce Clause. *Id.* A petition for a writ of certiorari is likewise being filed

in the *Midland Central* case today. The simultaneous pendency before this Court of these cases illustrates that not only is the "continuity of transit" issue recurring, but it implicates a far broader range of goods than natural gas. Industry, States, and local governments would all benefit from clarification.

2. The "Physical-Presence" Issue is Important and Recurring.

The Texas court concluded that the tax at issue violated the Commerce Clause because it did not satisfy the first prong of *Complete Auto* – "substantial nexus." App., *infra*, 21. Again, having concluded that the gas was in "continuity of transit" in interstate commerce, the court attached little significance to the large amounts of Peoples' gas that were continuously present in Harrison County, Texas. Rather than focus on the presence of the *gas* in storage in Harrison County – the object of the state ad valorem property tax – the court focused instead on the presence of the *taxpayer*: "Peoples maintains no office in Texas. Nor does it have any employees, representatives, or physical facilities in the State." *Id.*, at 19. Because the taxpayer was absent from the State, the Texas court found no substantial nexus. *Id.*, at 21.

In support of its *taxpayer*-focused (not *property*-focused) analysis, the Texas court invoked *Quill*'s "physical-presence" rule: "The Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence

in the state." App., *infra*, 19 (citing *Quill*, 504 U.S., at 312-14). *Quill* involved a sales and use tax – not a property tax. In *Quill*, this Court invoked *stare decisis* in declining to renounce the "physical-presence" rule in cases involving Commerce Clause challenges to sales and use taxation. 504 U.S., at 317-18. The Court thereby let stand a bright-line rule that the Court originally adopted a decade before *Complete Auto* in *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill.*, 386 U.S. 753, 758 (1967).

Again, the Supreme Court of Oklahoma was "unpersuaded by [the Texas] court's reasoning." *Missouri Gas,* 234 P.3d, at 959 n.84. The Oklahoma court rejected the notion that the taxpayer's *in personam* contacts with the State should control for an ad valorem tax on *property*. *Id.* Rather, the Oklahoma court concluded that the fundamental question should be whether the taxpayer *owns property* in the jurisdiction that seeks to impose the ad valorem tax: "While this case certainly presents some complexity, the fundamental question is simple: does the taxpayer own property located in the county seeking to impose the ad valorem tax?" *Id.* "Nothing in the Texas appellate court's decision persuades us that the answer to the correctly formulated question is anything other than a resounding yes." *Id.*

The relevance of the taxpayer's physical presence in the State outside the context of sales and use taxation needs to be clarified. *See Quill*, 504 U.S., at 312-14. One can envision an entire range of situations in which the taxpayer itself might not have an *in*

personam type of "physical presence" in the State, yet could nonetheless own real or personal property in the State that would otherwise be subject to ad valorem taxation. If (as the Texas court held but the Oklahoma court disagreed) such property is beyond the reach of state taxation simply because the taxpayer itself "maintains no office[,] employees, representatives, or physical facilities in the State" (App., *infra*, 19), the adverse impact on state taxing authorities could be incalculable.

The scope of *Quill*'s "physical-presence" requirement is a recurring issue on which state courts are divided. *See Lanco, Inc. v. Dir., Div. of Taxation*, 908 A.2d 176, 177 (N.J. 2006) ("Since the Court decided *Quill*, a split of authority has developed regarding whether the Supreme Court's ['physical-presence'] holding was limited to sales and use taxes. . . . We believe that the better interpretation of *Quill* is the one adopted by those states that limit the Supreme Court's holding to sales and use taxes."), *cert. denied*, 551 U.S. 1131 (2007). Another petition now pending before this Court raises this issue with regard to a state income tax. *See Asworth, LLC v. Dep't of Revenue, Finance, and Admin. Cabinet*, No. 10-662. The present case presents this recurring issue in a narrower, but no less important, context: whether the "physical-presence" rule precludes state taxation where the taxpayer has *property* in the State, and that property is itself the object of the ad valorem tax at issue.

C. This Case Warrants Immediate Review.

This case cleanly presents both the narrow constitutional issue and the two broader constitutional controversies out of which it arises. The competing views of the law have already been analyzed by the Solicitor General as well as the lower courts. Further delay would neither frame the constitutional issue more cleanly nor enhance presentation of the competing arguments. Rather, the delay would only result in continuing confusion, when all concerned desire certainty. This is why even industry opponents of the tax at issue agree with state taxing authorities that this is "a recurring issue that merits this Court's attention." AGA Amicus Brief (No. 08-1458), at 3.

II. The Decision Below is Erroneous.

Three errors in the court of appeals' analysis particularly deserve this Court's attention.

A. The Court of Appeals Erred in Using this Court's "Continuity of Transit" Analysis to Eclipse the *Complete Auto* Analysis.

The Texas court of appeals erroneously concluded that this Court's traditional "continuity of transit" analysis remains "crucial" to the Commerce Clause inquiry. App., *infra*, 13. As the Supreme Court of Oklahoma correctly concluded, that analysis has effectively been "superseded by the Supreme Court's

decision in *Complete Auto*." *Missouri Gas*, 234 P.3d, at 959 n.84.

Examples of this Court's cases employing the older "continuity of transit" analysis include *Blasius*, 290 U.S., at 9-12, and *Bacon v. Illinois*, 227 U.S. 504, 511-17 (1913). The Solicitor General explained the analysis employed in those cases: "Under that approach, the critical question was whether the interstate transit of goods had been sufficiently interrupted for purposes other than merely facilitating the transit; if so, the goods were deemed locally taxable." Br. for U.S. (No. 08-1458), at 9-10. Correspondingly, if the goods were determined to be "in transit in interstate commerce," they were deemed immune from state taxation. *See Blasius*, 290 U.S., at 9. Thus, under the traditional approach, "the 'crucial question' . . . is . . . 'continuity of transit.'" *Id.* (quoting *Carson Petroleum Co. v. Vial,* 279 U.S. 95, 101 (1929)). The question was "crucial" in that bygone era because it was determinative of the State's taxing power.

In contrast, after *Complete Auto*, deciding whether goods are *in* or *out* of the stream of interstate commerce – the objective of the "continuity of transit" test – is no longer determinative. In *Complete Auto*, this Court "rejected the notion that state taxes levied on interstate commerce are *per se* invalid." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 615 (1981) (citing *Complete Auto*, 430 U.S., at 288-89). Correspondingly, it is no longer true that determining goods to be *out* of the stream of interstate commerce necessarily means that they are locally

taxable. Rather, this Court has "long since rejected any suggestion that a state tax or regulation affecting interstate commerce is immune from Commerce Clause scrutiny because it attaches only to a 'local' or intrastate activity." *Id.*

In short, although the "continuity of transit" analysis was once determinative of the Commerce Clause inquiry, it no longer is. What is determinative today is whether the state tax satisfies the *Complete Auto* four-pronged test. If it does, "no impermissible burden on interstate commerce will be found." *Japan Line, Ltd. v. Los Angeles County*, 441 U.S. 434, 444-45 (1979). Thus, *Complete Auto* has effectively displaced the "continuity of transit" analysis, and the court below erred in granting the latter preeminence.

B. The Court of Appeals Erred in Applying *Quill*'s "Physical-Presence" Rule to Ad Valorem Property Taxation.

Having concluded that Peoples' gas was in "continuity of transit" in interstate commerce, the court of appeals attached little significance to the massive presence of Peoples' storage gas in Harrison County, Texas. Instead, the court supported its conclusion that the Commerce Clause prohibits the state tax at issue by noting that the taxpayer, Peoples, has no office, employees, representatives, or physical facilities in the State. App., *infra*, 19.

Yet the absence of such *in personam* contacts with the State is irrelevant when the tax at issue is

one on *property*. For a property tax, the constant physical presence of an inventory of the property in the State should be sufficient to satisfy the requisite link between the State and the property sought to be taxed. *See Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 777 (1992) (reciting as a "fundamental requirement of both the Due Process and Commerce Clauses that there be 'some definite link, some minimum connection, between a *state* and the . . . *property* . . . it seeks to tax'") (emphasis added) (quoting *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954)). The requisite connection between the *State* and the *property* in this case is substantial.

In holding otherwise, the Texas court of appeals erroneously invoked this Court's decision in *Quill*. App., *infra*, 19 (citing *Quill*, 504 U.S., at 312-14). In *Quill*, the Court declined to overrule the requirement that the taxpayer be physically present in the State to justify imposing a *sales* or *use* tax.

Quill is explicitly narrow, and should be confined to sales and use taxes. *Quill* makes clear that the "physical-presence requirement" originally adopted in *Bellas Hess* was "established for sales and use taxes," and that "we have not, in our review of other types of taxes, articulated the same physical-presence requirement. . . ." 504 U.S., at 314. Alternatively, if this Court concludes that the "physical-presence" rule does apply outside the context of sales and use taxation, the Court should hold that the physical presence of the taxpayer's property in the State suffices to satisfy the rule, at least if that property is the object

of the ad valorem tax at issue. In either event, the Court should hold that the "physical-presence" requirement does not prohibit the ad valorem tax in this case.

C. The Court of Appeals Erroneously Held that the State Tax at Issue Fails the *Complete Auto* Test.

The court of appeals held that the state tax at issue fails the first and fourth prongs of the *Complete Auto* test. App., *infra*, 22. The court was wrong; the tax satisfies both of those prongs.[6]

1. The Tax is on Property that Has a "Substantial Nexus" with Texas.

The first prong of *Complete Auto* requires that the tax be "applied to an activity with a substantial nexus with the taxing State." 430 U.S., at 279. This Court has stated that it is a requirement of both the Due Process Clause and the Commerce Clause that there be some definite link, some minimum connection between a *state* and the *property* it seeks to tax. *Allied-Signal*, 504 U.S., at 777. *Property* – a large inventory of natural gas owned by Peoples and held in underground storage in Harrison County, Texas –

---

[6] The tax satisfies the second and third prongs as well. But because the court of appeals did not address those two prongs in its opinion, the Appraisal District does not address them in this petition.

is what the Appraisal District seeks to tax here. Although volumes of Peoples' gas may come and volumes of gas may go, on any given day Peoples has in storage in Texas what can only be described as a massive inventory of natural gas. There is "substantial nexus" between that storage gas and the State of Texas, which suffices for the ad valorem tax at issue to survive constitutional scrutiny.

Professor Hellerstein agrees, concluding with specific regard to this case: "The physical presence of a 'significant volume' of the owner's property appears to be more than sufficient to constitute 'substantial nexus.'" Hellerstein & Hellerstein, *supra*, ¶ 4.13[3][a]. He found the court of appeals' holding to the contrary to be "highly questionable, if not plain error." *Id.*

The Solicitor General similarly concluded that "the nexus between Oklahoma and the 'large volumes of gas' stored there 'for a substantial part of the year' is sufficient to satisfy prong one of the *Complete Auto* test." Br. for U.S. (No. 08-1458), at 21. Exactly the same thing can be said of the large volumes of gas stored in Texas.

A property's mere physical presence in the State may not always suffice to establish "substantial nexus." The Solicitor General provided an example of an exception in *Missouri Gas*: "[T]he transportation of natural gas could be significantly burdened if multiple States attempted to tax the same volume of gas based solely on its movement through an interstate pipeline." Br. for U.S. (No. 08-1458), at 19. In light of this concern, the Supreme Court of Oklahoma limited

its holding to *storage* gas: "[C]oncluding that the natural gas at issue bore a constitutionally sufficient nexus to the taxing State, the Oklahoma Supreme Court carefully limited its holding to *stored* natural gas." *Id.*, at 19 n.6 (emphasis in original) (quoting *Missouri Gas*, 234 P.3d, at 954 (concluding that "[petitioner's] storage gas cannot be characterized as goods that are merely passing through the state")). A similarly limited holding in this case would not open the door to State taxation of commodities in pipelines.

2. The Tax is "Fairly Related to the Services Provided by the State."

The fourth prong merely requires that the tax be "fairly related to the services provided by the State." *Complete Auto*, 430 U.S., at 279. "The simple but controlling question is whether the state has given anything for which it can ask return." *Commonwealth Edison*, 453 U.S., at 625 (internal quotation marks omitted).

Consistent with these authorities, the Oklahoma Supreme Court correctly addressed the fourth prong in a manner applicable here:

> The tax in this case operates on the presence of personal property in Woods County. It is taxed to the same extent as all other personal property in the county. [Taxpayer] MGE is therefore being asked to shoulder no more than its fair share for the support of government-provided services and the receipt of "the advantages of a civilized society."

Missouri Gas, 234 P.3d, at 959 (quoting *Exxon Corp. v. Wisconsin Dep't of Revenue,* 447 U.S. 207, 228 (1980), quoting *Japan Line*, 441 U.S., at 445).

In contrast, the Texas court of appeals incorrectly focused on Pipeline's facility and cushion gas – not Peoples' working gas:

> While we do not doubt the value of [the] services [provided within the county], we note, again, that services such as law enforcement and the fire department would serve the North Lansing facility itself, and the facility undoubtedly belongs to Pipeline, which does pay ad valorem taxes on both the "cushion" gas it maintains in the facility and the physical plant of the facility itself.

App., *infra*, 21-22.

That Pipeline pays ad valorem taxes on its "cushion" gas and "the physical plant of the facility itself" in no way suggests that Peoples' *working* gas should be constitutionally excused from taxation. Peoples benefits from the storage of its working gas in Harrison County, and it should be no less responsible for ad valorem taxation of its working gas than Pipeline is for taxation of its cushion gas. Because Peoples substantially benefits from the storage of its gas, it "may be required to contribute to the cost of providing *all* governmental services, including those services from which it arguably receives no direct 'benefit.'" *Commonwealth Edison*, 453 U.S., at 628 n.16 (emphasis in original).

That Pipeline's "physical plant of the facility itself" is taxed (App., *infra*, 22) is immaterial. The need for fire protection, for example, arises not from the physical plant itself so much as it does from the billions of cubic feet of natural gas stored within the facility.

As with the first prong, Professor Hellerstein concluded that the court of appeals' decision regarding the fourth prong is "highly questionable, if not plain error." Hellerstein & Hellerstein, *supra*, ¶ 4.13[3][a]. He sees "no basis for the conclusion that the taxpayer's gas does not receive 'police and fire protection . . . and the advantages of a civilized society.'" *Id.* This Court should reach the same conclusion.

CONCLUSION

The Court should grant the petition for writ of certiorari.

Respectfully submitted,

DOUGLAS W. ALEXANDER
Counsel of Record
AMY WARR
ALEXANDER DUBOSE & TOWNSEND LLP
515 Congress Avenue
Suite 2350
Austin, Texas 78701
(512) 482-9300
dalexander@adtappellate.com

ROGER TOWNSEND
ALEXANDER DUBOSE & TOWNSEND LLP
1844 Harvard Street
Houston, Texas 77008
(713) 523-2358

ROY T. ENGLERT, JR.
ROBBINS, RUSSELL, ENGLERT, ORSECK, UNTEREINER & SAUBER LLP
1801 K Street, N.W.
Suite 411
Washington, D.C. 20006
(202) 775-4500

KIRK SWINNEY
MCCREARY, VESELKA, BRAGG & ALLEN, P.C.
700 Jeffrey Way, Suite 100
Round Rock, Texas 78665
(512) 323-3200