COMPACTS, CARTELS, AND CONGRESSIONAL CONSENT

Michael S. Greve[1]

The Compact Clause (Art. I, Sec. 10 U.S. Constitution) requires congressional approval for "any agreement or compact" among the states. In the teeth of this wording, the Supreme Court held, in U.S. Steel Corp. v. Multistate Tax Commission, *(1978), that the Clause applies only to state compacts that "encroach" upon federal supremacy. Courts have followed this precedent in sustaining the 1998 Multistate Agreement on tobacco litigation ("MSA") against Compact Clause challenges.*

Compacts, Cartels, and Congressional Consent *argues that* U.S. Steel *was wrongly decided. Congressional "negatives," including the Compact Clause, invert the default rule for constitutionally suspect classes of state laws. Whereas ordinary state laws are permitted to go into (and remain in) effect unless and until Congress or the courts exercise their authority under the Supremacy Clause, congressional negatives render state laws inoperative unless and until Congress takes affirmative action. By limiting the operation of the Compact Clause to state agreements that encroach on federal supremacy—which are unlawful in any event—the Supreme Court has re-inverted the constitutional presumption and emptied the Compact Clause of all content.*

This Article explains the forgotten constitutional logic and wisdom of the Compact Clause and argues for a Compact Clause jurisprudence that will safeguard constitutional purposes (in particular, the protection of equality and comity among the states). It shows that both the 1967 Multistate Tax Compact considered in U.S. Steel *and the 1998 tobacco settlement are clearly unconstitutional without congressional consent. It concludes that a re-invigorated Compact Clause is consistent with principled, constitutional federalism doctrines.*

---

[1] For helpful comments on an earlier draft I am indebted to Jonathan H. Adler, Martha Derthick; Richard A. Epstein, Robert Gasaway; Edward W. Warren, and Stephen F. Williams. All errors etc. are mine.

I. INTRODUCTION

A. The Upside-Down, Inside-Out Compact Clause

On November 17, 1998, the attorneys general of 46 states and the major U.S. tobacco manufacturers signed an agreement governing the sale of cigarettes and other tobacco products in the United States. The so-called Master Settlement Agreement (MSA), which ended an unprecedented state litigation campaign against the industry, provides for the companies' payment of nearly a quarter of a trillion dollars, over a period of twenty-five years, in "damages" and other payments to the states.[2] In all but name, the

[2] The MSA cannot be found in any law library or statute book. It is, however, available at http://www.naag.org/tobac/cigmsa.rtf. All references hereinafter are to the on-line text.

payments are a national consumption tax, paid almost entirely by individual smokers.[3] No legislator at any level of government ever voted for (or against) that tax. The United States Congress did not approve the MSA.

The Compact Clause of Article I, Section 10 of the Constitution provides that "[n]o State shall, *without the Consent of Congress* … enter into any Agreement or Compact with another State, or with a foreign Power."[4] The MSA bears the signatures of 46 state attorneys general and, by its terms, requires approval by eighty percent of the signatory states for its full implementation.[5] It would thus appear to be a state "agreement" and, as such, require congressional consent. In several lawsuits over the MSA, however, federal courts have dismissed Compact Clause claims, uniformly without extended discussion.[6]

Perplexing at first sight, these rulings rely on Supreme Court precedents that have held, occasionally *in haec verba*, that the Compact Clause cannot possibly mean what it says.[7] The leading modern case, *U.S. Steel Corp. v. Multistate Tax Commission*,[8] arose

---

[3] *See infra* nn. , accompanying text, and sources cited *id.*

[4] U.S. Const. Art. I Sec. 10 cl. 3 (emphasis added).

[5] MSA II(u).

[6] In the leading appellate case, the court discussed the merits of plaintiff's Compact Clause claim in five short paragraphs. *Star Scientific, Inc. v. Beales*, 278 F.3d 339, 359-60 (4th Cir. 2002). For a similarly cursory dismissals *see, e.g., PTI Inc. v. Philip Morris Inc.*, 100 F.Supp. 2nd 1179, 1198 (C.D. Cal. 2000); One court characterized the plaintiffs' (poorly pled) Compact Clause claim as "plainly frivolous": *Hise v. Philip Morris, Inc.*, 46 F.Supp.2d 1201, 1210 (N.D.Ok. 1999), *aff'd*, No. 99-5113, 2000 U.S. App. LEXIS 2497 (10th Cir.), *cert. denied*, 121 S.Ct. 384 (2000).

[7] The most important pronouncement to this effect is *Virginia v. Tennessee*, 148 U.S. 503, 519 (1893) (discussed *infra* nn. and accompanying text). In the same spirit, the Court has classified particular interstate arrangements as not really "compacts" in the relevant sense. *Bode v. Barrett*, 344 U.S. 583 (1953); *Massachusetts v. Missouri*, 308 U.S. 1 (1939); *S.F.R. v. James*, 161 U.S. 545 (1896) (all holding that reciprocity agreements do not constitute compact within the meaning of the Compact Clause); *Northeast Bancorp v. Bd. Of Governors of Fed. Reserve Sys.*, 472 U.S. 159, 175 (1985) (affirming that position, though possibly in *dictum—see infra* n.). The Court has also held that congressional consent

over a convoluted multi-state arrangement governing the taxation of interstate business income. In sustaining the arrangement against a Compact Clause challenge, the Supreme Court read the Clause, in the teeth of its language, to require congressional approval only when a state compact impinges upon the supremacy of the United States. Since such compacts are bound to be void in any case under a conventional constitutional or preemption analysis, it is difficult to imagine a state agreement on which the Compact Clause would operate as a distinct constitutional requirement and obstacle.

Extant compacts and their fate in the courts illustrate the emasculation of the Compact Clause. Prior to 1921, 36 compacts between states were put into effect with the consent of Congress; virtually all of these settled boundaries between contiguous states.[9] Modern compacts, in contrast, often address "tough national issues"[10] and establish expansive (and expensive) regulatory regimes. The 200-odd state compacts now in effect (excluding boundary agreements) cover a broad range of issues, from to environmental and energy policy (39 compacts) to water allocation (38), traffic and transportation (28), crime control (16), and education (12), among other matters.[11] Many compacts are

---

may be implied from congressional acquiescence: *Poole v. Fleeger*, 36 U.S. (11 Pet.) 185, 209 (1837); *Green v. Biddle*, 21 U.S. (8 Wheat.) 1, 85-87 (1823); *Virginia v. West Virginia*, 78 U.S. 39 (1878); *Virginia v. Tennessee*, 148 U.S. 503, 521 (1893). For a brief discussion of the form and timing of congressional consent *see infra* nn. and accompanying text.

8 434 U.S. 452 (1978).

9 **Cite Warren**. *See also* Brevard Crihfield, *Interstate Compacts, 1783-1977: An Overview*, THE BOOK OF THE STATES 1978-79, at 580 (Council of State Governments, 1978). The one exception was the separation of West Virginia from Virginia in 1862. *Id.*

10 Edward D. Feigenbaum, *Interstate Compacts and Agreements*, 26 THE BOOK OF THE STATES 453 (Council of State Governments, 1986).

11 The figures are derived from WILLIAM KEVIN VOIT, INTERSTATE COMPACTS & AGENCIES, 1998 (Council of State Governments, 1998). An alphabetical listing, *id.* at 11-14, shows 192 compacts; the descriptive portion of the report, at 15-133, shows 208 compacts. In addition, the report lists, at 159-60, 51 compacts that "may be" dormant or defunct.

administered, on an on-going basis, by standing compact boards or commissions.[12] While most compacts operate with congressional consent (and, in a few instances, subject to periodic renewal requirements),[13] some compacts have gone into effect without receiving congressional approval. The Multistate Tax Compact sustained in *U.S. Steel,* as well as the 1998 Master Settlement Agreement on tobacco litigation, both went into effect after—and despite—unsuccessful attempts to obtain congressional consent.[14] The judicial decisions that have to date sustained those arrangements fit a consistent pattern: even though most compact litigation seems to have arisen over unapproved compacts,[15] it appears that no court has ever voided a state agreement for failure to obtain congressional consent.[16]

This Article argues that the judiciary should enforce the Compact Clause. The constitutional text alone might appear sufficient to sustain that argument: if the plain words of the Compact Clause mean anything, they must mean that state agreements of the scale, complexity, and consequence of the MTC or the MSA require congressional

---

12 A precise count is hard to come by. *Voit*, *supra* n. 11, at 157-58, lists 116 compact authorities, boards, commissions, and committees. While some of these bodies may be dormant or defunct, *id.* at 157, some existing multistate bodies may have been omitted from the list.

13 *See, e.g.*, Interstate Compact to Conserve Oil and Gas, 49 Stat. 939 (1935).

14 *See infra* nn. and accompanying text (MTC); *infra* nn. and accompanying text (MSA). By way of further examples, *see* David E. Engdahl, *Characterization of Interstate Arrangements: When is a Compact not a Compact?* 64 MICH L. REV. 63, 70-71 (1965) [hereafter Engdahl, "Interstate Arrangements"] (providing examples and describing states' increased insistence that certain types of compacts do not require congressional approval).

15 *Seattle Master Builders v. Pacific Northwest Electric Power & Conservation Council*, 786 F.2d 1359, 1374 (9th Cir. 1986)(Beezer, J., diss.); *cert denied*, 479 U.S. 1059 (1987).

16 Engdahl, *Interstate Arrangements*, 64 MICH. L. REV. at 69 (1965) ("[I]n every case since Virginia v. Tennessee in which an interstate arrangement has been challenged for lack of congressional consent, it has been held exempt from the consent requirement" (footnote citing cases omitted)). Thirty-plus years later, the statement is still accurate.

consent. The record of judicial obtuseness and scholarly indifference,[17] however, warrants a more elaborate effort to recover the forgotten constitutional logic and purpose of the Compact Clause and its place in the federal architecture. The Compact Clause—a species of the congressional "negative" James Madison urged upon the Constitutional Convention[18]—inverts the general constitutional default rule for state enactments: whereas the ordinary supremacy arrangement of the Constitution allows state laws to become and remain effective until a court enjoins or Congress preempts them, the Compact Clause renders state enactments within its range *in*effective unless and until Congress affirmatively validates them. By reserving the application of that rule to compacts that compromise federal supremacy, the Supreme Court has effectively re-inverted the default rule and brought state agreements under the very supremacy arrangement from which the Compact Clause exempts them.

That move constitutes a twofold constitutional error. The Compact Clause merits judicial respect not only because it is the constitutional default principle but also because it is the *correct* principle. Congressional approval for all state agreements, or something very close to it, is the only compact rule that is consistent with constitutional federalism.

B. Function and Form

A jurisprudence that has turned the Compact Clause on its head is, in its own way, a considerable judicial achievement. The case law through which this was accomplished,

---

[17] The literature on the Compact Clause is slim. To my knowledge, not a single law review article or textbook published during the past half-century has criticized the judicial emasculation of the Clause as questionable, let alone clearly erroneous.

[18] *See infra* nn. and accompanying text.

summarized in Part II. of this Article, abounds with simple interpretive errors, as well as a great deal of judicial disingenuousness. But the fuel that propelled the case law on its ill-fated trajectory was an interpretive shift from the text and form of the Compact Clause to its purpose and function—or, more precisely, a gross misunderstanding of its function. From the actual Compact Clause, whose uncompromising language leaves no doubt about the Founders' "deep-seated and special fear of agreements between States,"[19] scholars and judges shifted to a functional view of interstate compacts as an efficient and underutilized institutional arrangement.[20] Their arguments come in full federalist regalia and portray state compacts as a pristine and constitutionally favored example of cooperative federalism in action.[21]

---

19 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 489 (White, J., dissenting).

20 *See, e.g.*, Felix Frankfurter & James Landis, *The Compact Clause of the Constitution—A Study in Interstate Adjustments*, 34 Yale L. J. 685 (1925) [hereafter "The Compact Clause"]; VINCENT V. THURSBY, INTERSTATE COOPERATION: A STUDY OF THE INTERSTATE COMPACT 149 (1953) (recommending compacts as a means to protect the vitality of the states and to relieve overburdened national government); FREDERICK ZIMMERMAN & MITCHELL WENDELL, THE INTERSTATE COMPACT SINCE 1925, 126 (1951) ("The interstate compact is a strong legal instrument for expanding cooperative federalism in situations to which other cooperative methods are not as applicable."); Richard C. Kearney & John J. Stucker, *Interstate Compacts and the Management of Low Level Radioactive Wastes*, 45 PUB. ADMIN. REV. 210, 214 (1985) (interstate compacts an effective means to protect state sovereignty and cooperation where national government remains inactive); Jo M. Ferguson, *The Legal Basis for a Southern University—Interstate Agreements Without Congressional Consent*, 38 KY L. J. 347 (1950); Note, *To Form a More Perfect Union? Federalism and Informal State Cooperation*, 102 HARV. L. REV. 842 (1989).

21 State officials and the leaders of state lobbying and umbrella organizations, such as the Council of State Governments and the National Association of Attorneys General, have been especially ardent in celebrating state compacts as a federalist arrangement *par excellence* and in denouncing perceived or real congressional interferences. For a particularly strident example of states-rights chauvinism *see* Ferguson, supra n. 20. *See also* Feigenbaum, *supra* n. at 453 (Compact Clause intended to "facilitate" state agreements); and Robert G. Dixon, Jr., *Constitutional Bases for Regionalism: Centralization; Interstate Compacts; Federal Regional Taxation*, 33 GEO. WASH. L. REV. 47, 65 (1964) ("As a matter of first impression, it could be argued that the intent of the Framers … was to *enable* the states, by consent, to take joint action to solve problems which lay beyond the power and capacity of any one state. " (emph. added) (describing state officials' views)). One might as well argue that the Founders intended to "facilitate" and "enable" state duties on imports and exports by subjecting such imposition to approval by Congress. *See* U.S. Const. Art. I Sec. 10 Cl. 2.

This intellectual tradition reaches back to an impressive 1925 law review article by (later) Justice Felix Frankfurter and James M. Landis, which celebrated "the imaginative adaptation of the compact idea" to increased regionalism and "[t]he overwhelming difficulties confronting modern society."[22] While Frankfurter and Landis did not argue for dispensing with the congressional consent requirement (quite the opposite),[23] they furnished the intellectual apparatus—and the soothing rhetoric of cooperation, flexibility, and localism—that later generations of scholars and judges would put to that purpose.[24] Their cheerful endorsement of state compacts partook of a broader, intellectual and political effort to portray America's traditional, "dual" federalism as archaic and doctrinaire. The needs of a modern, complex, industrial society, the Progressives and their New Deal heirs argued, command government improvisation, experimentation, and cooperation. The New Deal and, after initial resistance, the Supreme Court embraced the best-known and perhaps most consequential form of "cooperative federalism"—vertical power- and revenue-sharing arrangements between the states and the national government.[25] The embrace of horizontal federalist cooperation among states—regardless of constitutional strictures—followed the same

---

22 Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 729 (1925).

23 Since state agreements may affect non-party states, "Congress *must* exercise national supervision through its power to grant or withhold consent, or to grant it under appropriate conditions. The framers thus astutely created a mechanism of legal control over affairs that are projected beyond state lines and yet may not call for, nor be capable of, national treatment." Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. 685, 694 (emph. added). *Justice* Frankfurter apparently considered congressional approval *de rigeur* for all state compacts. *West Virginia ex rel. Dyer v. Sims*, 341 U.S. 22, 27 (1951).

24 *Cf. Seattle Master Builders v. Pacific Northwest Electric Power & Conservation Council*, 786 F.2d 1359, 1364 (9th Cir. 1986); *cert denied*, 479 U.S. 1059 (1987) (Frankfurter & Landis article "set[s] the tone for the modern use of compacts.")

25 The standard account of the transition from dual to cooperative federalism is Edward S. Corwin, *The Passing of Dual Federalism*, 36 VA L. REV. 1 (1950). *See also* EDWARD S. CORWIN, THE TWILIGHT OF THE SUPREME COURT (1934).

political and judicial trajectory. The Supreme Court sustained state agreements against a variety of challenges[26] and, moreover, affirmatively encouraged states to utilize compacts as a means of resolving boundary disputes, water rights questions, and pollution problems.[27] By 1959, the Court waxed approvingly about "imagination and resourcefulness in devising fruitful interstate relationships" and about the "voluntary and cooperative actions of individual states with a view to increasing harmony within the federalism created by the Constitution."[28]

The most persuasive defense of this interpretation rests on what we now call a transaction cost model. Federalism poses problems of coordination (such as interstate pollution) and scale (such as the management of natural resource systems that span state jurisdictions).[29] Bargaining by the affected states may provide a more efficient solution to such problems than the alternative available channels—litigation, or centralized, federal legislation and regulation.[30] From this vantage, the constitutional requirement of

---

[26] *See, e.g.*, *Hinterlider v. La Plata Co.*, 304 U.S. 92 (1938) (compact trumps private appropriation rights guaranteed by state Constitution); *West Virginia ex rel. Dyer v. Sims*, 341 U.S. 22 (1951) (sustaining compact against allegedly conflicting state constitutional claims).

[27] *See, e.g.*, *Colorado v. Kansas*, 320 U.S. 383, 392 (1943). Perhaps the earliest such encouragement can be found in *New York v. New Jersey*, 256 U.S. 296, 313 (1921) ("[T]he grave problem of sewage disposal … is one more likely to be wisely solved by cooperative study and by conference and mutual concession on the part of … the States so vitally interested in it than by proceedings in any court however instituted"). *See also* West Virginia *ex rel* Dyer v. Sims, 341 U.S. at 27 (1951) (quoting that language).

[28] *New York v. O'Neill*, 359 U.S. 1, 6 (1959). While Justice Frankfurter wrote those stirring words, for a unanimous Court, in the course of rejecting a challenge to a reciprocity agreement under the Fourteenth Amendment (but not the Compact Clause), his pronouncement has been quoted approvingly in compact cases. *See, e.g.*, *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 470 (1978).

[29] *See, e.g.,* Gordon Tullock, *Federalism: Problems of Scale*, 6 PUB. CHOICE 19 (1964); Richard O. Zerbe, *Optimal Environmental Jurisdictions*, 4 ECOLOGY L. Q. 193 (1974); Dale D. Goble, *The Compact Clause and Transboundary Problems: "A Federal Remedy for the Disease Most Incident to a Federal Government,"* 17 ENVTL. L. 785 (1987).

[30] Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 705-08.

congressional approval for state agreements seems dysfunctional. In addition to creating delay and uncertainty, Congress might hold sensible and efficient state bargains hostage to logrolling and rent-seeking. Experience has also shown that Congress may impose onerous conditions on state compacts and their administrators, thus dissipating the gains from flexibility and local control that compacts may produce.[31] So long as Congress and the Supreme Court remain free to superintend and, if need be, void interstate compacts, "there is no danger of any misuse of the States' sovereign powers in their agreements with each other."[32]

Contrary to this sanguine account, however, interstate compacts pose four serious institutional risks: (1) state bargaining with federal rights and prerogatives and, consequently, infringements on the interests of the United States; (2) third-party externalities, meaning infringements on the rights and interests of non-compacting states; (3) cartelization, meaning the creation, through compacts, of institutional regimes and arrangements that restrict policy competition among the states;[33] and (4) agency problems, including the transfer of state authority to unaccountable, irresponsible, extra-constitutional institutions. Since these risks affect even the most tenable (Coasean) account of state bargaining, the functional view of the Compact Clause is untenable on its own terms. But the risks just listed are not somehow separate and apart from the Compact

---

[31] Brevard Crihfield, *The States and the Council of State Governments*, 35 STATE GOV'T 20, 65 (1962); Robert C. Elickson, *Public Property Rights: A Government's Rights and Duties When Its Landowners Come into Conflict with Outsiders*, 52 S. CAL. L. REV. 1627, 1654-55 (1979).

[32] Ferguson, *supra* n. 20 at 359.

[33] The suppression of policy competition has been described as a potential virtue and advantage, rather than a problem, of state compacts. *See, e.g*., Jill Elaine Hasday, *Interstate Compacts in a Democratic Society: The Problem of Permanency*, 49 FLA. L. REV. 1, 7 (1997); Note, *To Form a More Perfect Union? Federalism and Informal State Cooperation*, 102 HARV. L. REV. 842 (1989). For reasons explained *infra* nn. and accompanying text, this view rests on a misunderstanding of the purpose of a federal Constitution.

Clause; they are jazzed-up versions of the dangers that the Founders contemplated in enacting the Clause. Extant Compact Clause doctrine, in contrast, acknowledges only the first risk, and even that only in a highly attenuated form. It is oblivious to the risks of interstate externalities and exploitation, and it encourages the states to create, through the establishment of supra-state agencies, a Constitution parallel to the one we have.[34]

State compacts, then, may enhance efficiency and federalism values, but they may also compromise those values. A "federalism" that celebrates the exercise of state sovereignty, in derogation of the Constitution and at the risk of diminishing political accountability and the rights of non-compact states, is federalism fubar—[messed] up beyond all recognition. That is the easy part of the analysis. The hard part is to distinguish between efficient compacts and those that inflict unwarranted costs on third parties (states, citizens, or the United States) and then to figure out a constitutional rule

---

[34] Since I will return to the theme of unapproved state compacts as a means of establishing an alternative Constitution (*see infra* nn. , nn. , and accompanying text), it is worth noting that others have perceived that potential—and not always as a menace. In 1937, the Council of State Governments, an interstate body established for the promotion and administration of state compacts, passed an ominously entitled "Declaration of Interdependence," beginning as follows:

> When, in the course of human events, it becomes necessary for a nation to repair the fabric which unites its many agencies of government, and to restore the solidarity which is vital to orderly growth, it is the duty of responsible officials to define the need and to find a way to meet it. …
>
> Through established agencies of cooperation, through uniform and reciprocal laws and regulations, *through compacts under the Constitution*, through informal collaboration, and through all other means possible, our nation, our states, and our localities must fuse their activities with a new fervor of national unity.

BOOK OF THE STATES II, 143-44 (Council of State Governments and American Legislators' Association, 1937) (emphasis added). For a similar What's-a-Constitution-Among-Friends celebration of "extraconstitutional forms of legal invention" and the "interplay of living forces of government to meet the evolving needs of a complex society" *see New York v. O'Neill*, 359 U.S. 1, 10-11 (1959).

that promises *ex ante*, over the long haul and the general run of cases, to minimize the aggregate costs of institutional error on either side.[35]

One obvious candidate is the actual Compact Clause: *no* state agreement or compact without congressional consent, period. On this textualist view, all that remains is to define the essential elements of the Clause—what constitutes a "compact" and an "agreement"; what constitutes a compact or agreement of and by the state (as distinct from its officers or the state's acts in a proprietary, non-sovereign capacity);[36] and what constitutes timely congressional consent.[37] As already suggested, the case for enforcing the Compact Clause as written is to my mind highly persuasive. Nonetheless, I will also articulate and defend a slightly more limited interpretation: a challenge to a state compact for lack of congressional consent should prevail if the plaintiffs establish a credible case that the challenged state agreement implicates one or more of the four specific risks identified above.[38]

---

[35] The Supreme Court has tended to focus on the likely effects of each individual compact submitted for its consideration: Engdahl, *Interstate Arrangements*, 64 MICH L. REV. 63, 68 (1965). This *ex post* perspective misconceives the constitutional enterprise.

[36] The prevailing view, which I believe to be generally correct, holds that the Compact Clause extends only to compacts that involve the exercise of sovereign state power. Engdahl, *Interstate Arrangements*. 64 MICH. L. REV. 63, 88 n. 131 (1965). *But see* Edward T. Swaine, *Negotiating Federalism: State Bargaining and the Dormant Treaty Power*, 49 DUKE L. J. 1127, 1270 (2000) (arguing that the distinction between "proprietary" and "sovereign" state actions "may be neither doctrinally sound nor easy to administer" (footnote omitted))(hereafter Swaine, *Negotiating Federalism*).

[37] *See infra* nn. and accompanying text.

[38] As further explained *infra* nn. and accompanying text, the proposed test turns on an examination of certain *types* of state compacts, rather than the effect or purpose of individual compacts. For instance, the test would require congressional consent for a state cartel-by-compact even if the cartel's empirical effects could be shown to be *de minimis*. For a similar approach to state bargaining with foreign governments—an issue with obvious structural similarities to the domestic Compact Clause—*see* Edward T. Swaine, *Negotiating Federalism*, 49 DUKE L. J. at 1261 (2000) (arguing for an "act-oriented approach [that] tries to delimit a class of activities that exceeds the limits of state authority under the Constitution, eschewing any attempt at measuring effects, balancing, or focusing on governmental purpose.").

The reasons for exploring this "functional" test are pragmatic. Cooperative state compacts and agreements have become an entrenched and judicially favored practice. In urging a re-examination and reversal, one is well-advised to push the argument for change no further than is necessary to avert serious, identifiable risks to constitutional norms and values—not only in the interest of political feasibility and legal continuity, but also because abrupt doctrinal adjustments tend to produce undesired and often paradoxical consequences.[39] Modern Compact Clause theory, such as it is, is avowedly functional, not textual, and once that judicial move has been made, a persuasive attempt to confront the functional interpretation on its own terms seems a more promising argumentative strategy than foot-stomping textualism. With any luck, a re-interpretation on shared theoretical ground will generate a rule that more closely approximates the original constitutional norm. In the case at hand, the approximation proves close enough for comfort: a serious functional Compact Clause turns out to be a thoroughly Madisonian construct.

C. Outline

Part II of this Article provides a brief overview of the historical development and the current state of Compact Clause doctrine. Part III outlines the forgotten constitutional logic of the Compact Clause, while Part IV applies that logic to a transaction model of state compacts. Parts V and VI illustrate the seriousness of the risks posed by state

[39] These consequences arise principally from the fact that political institutions, including courts, may respond to new and improved rules in unexpected ways. *See, e.g.*, Adrian Vermeule, *Does Commerce Clause Review Have Perverse Effects?* 46 VILL. L. REV. 1325 (2001) (arguing that "decentralizing" Commerce Clause decisions may induce centralization). A literal Compact Clause interpretation might well produce such effects: confronted with a rule that requires congressional approval for all state agreements and compacts, courts would further narrow the definition of what constitutes an agreement or compact for

compacts with, respectively, the 1967 Multistate Tax Compact of *U.S. Steel* fame and the 1998 Master Settlement Agreement between the states and tobacco manufacturers. Both agreements are unconstitutional under any reasonable reading of the Compact Clause. Part VII sketches a functional Compact Clause doctrine that would account for those risks without unduly compromising useful state cooperation. The Part compares that functional account to its close textual cousin and, moreover, argues that the judicial enforcement of the congressional consent requirement—especially in the proposed functional version—is consistent with the contemporary Supreme Court's federalism doctrines. The concluding Part VIII argues that a Compact Clause revival is not only urgent but also possible. In fact, such a revival presents an opportunity to strengthen the Supreme Court's federalism, and ours.

II. From Text to Farce

For a federal republic, and especially for a nascent federal republic, the prospect of separate, unsupervised agreements among its member-states and with foreign nations must constitute a cause for alarm. One obvious threat is dissolution through sedition and secession—which, as we have learned, states are more likely to commit collectively than individually.[40] A second threat is that states—of unequal size but equal sovereignty—may through cooperation imperil the interests of a sister-state.

---

constitutional purposes. The functional interpretation urged in this Article seems less likely to prompt such a response.----------

[40] Of course, the Confederate states—in keeping with their theory of the Constitution as a "Compact" among the states—seceded individually, not as a confederacy. States' rights advocates understood very well that a separate state compact within a federal republic was a perfect absurdity. Secession had to come first. That accomplished, the Confederacy forbade internal state compacts as

The Founders were painfully aware of these dangers. The Articles of Confederation barred any state from "enter[ing] into any confe[r]ence, agreement, alliance, or treaty" with foreign powers "without the Consent of the United States, in Congress assembled."[41] Likewise, the Articles required congressional consent for "any treaty, confederation, or alliance whatever" between the states[42] and provided that the Congress shall be the last resort in disputes and differences between the states.[43] These arrangements, however, proved inadequate to prevent disruptive controversies over ill-defined boundaries, discrimination by some states against sister states, and infringements on the United States through state treaties and agreements—with foreign nations, Indian tribes, and among the states—without the consent of the Congress.[44]

The Founders responded to these problems by strengthening the national government's authority and, simultaneously, by explicitly precluding the exercise of certain powers by the states. Article I of the Constitution enumerates the powers of Congress, and, in its final Section 10, denies specific powers to the states. The first paragraph lists powers that the states may not exercise under any circumstances (*i.e.*, with or without the consent of Congress), beginning with the provision that "No State shall enter into any Treaty, Alliance, or Confederation." The better-known injunctions against

---

absolutely as treaties, save for a narrow exception for cooperative navigational improvements of interstate waterways. Articles of the Confederate States of America art. I, sec. 10, cl. 3.

41 Art. of Confederation art. VI sec. 1.

42 Art. VI sec. 2.

43 Art. IX sec. 2.

44 For James Madison's account of these problems *see* his *Preface to the Debates in the Convention*, in NOTES OF DEBATES IN THE FEDERAL CONVENTION OF 1787 at 14 (Koch ed. 1984). Swaine, *Negotiating Federalism*, 49 DUKE L. J. at 1174-1181, 1198-1210 provides an instructive discussion of state interferences with "national" interests and diplomatic initiatives under the Articles of Confederation.

bills of attainder, the coinage of money, ex post facto laws, and laws impairing the obligation of contract are also listed here. The second and third paragraphs of Section 10 list powers that the states may not exercise *without the consent of Congress*. The second paragraph provides that "No State shall, without the consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing it's inspection Laws." The third paragraph, containing the Compact Clause, provides in full:

> No State shall, without the Consent of Congress, lay any duty of Tonnage, keep Troops, or Ships of War in time of Peace, enter into any Agreement or Compact with another State, or with a foreign Power, or engage in War, unless actually invaded, or in such imminent Danger as will not admit of delay.

The context of the Compact Clause clearly evidences the Founders special concern over state agreements. Agreements and compacts are subsumed under an injunction covering practices that constitute manifest threats to the Union and the Constitution—standing (state) armies, warfare, and actions conducive thereto; and duties of tonnage—like duties on imports and exports, a species of the state protectionism that so gravely concerned the Founders. Moreover, the constitutional language of the Compact Clause is broad and unqualified. A deal among states, or between a state and a foreign nation, is either a "treaty" (etc.), in which case it is absolutely prohibited; or else, it is a "compact" or "agreement" of some other kind, in which case it requires congressional approval. The constitutional text leaves no room for an argument that the Founders intended the Compact Clause to apply only to certain kinds of interstate agreements.

The "all-embracing"[45] nature of the Compact Clause has always been recognized with respect to state agreements with foreign nations. As Chief Justice Taney put it in *Holmes v. Jennison* (1840), a case arising over an extradition arrangement between the governor of Vermont and a Canadian official, the constitutional injunction against "*any* Agreement or Compact" appears to "prohibit every agreement, written or verbal, formal or informal, positive or implied, by the mutual understanding of the parties."[46] It is not entirely clear whether Taney derived his comprehensive understanding from the text of the Compact Clause itself or from an extra-textual "one voice" rationale for foreign relations—that is, a presumption that the Founders intended the nation to speak with a single, authoritative voice to other nations, leaving no room for the states in that arena.[47] (The phrase just quoted is preceded by a claim that the framers "anxiously desired to cut off all connection or communication between a state and a foreign power.")[48] The text of the Clause, of course, treats state agreements with foreign powers on a par with state-to-state agreements. If it compels a rigid interpretation in the foreign dimension, it compels an equally rigid, forbidding interpretation in its domestic dimension. Even at the time, though, that reading seemed counterintuitive. States had concluded boundary agreements and made arrangements for public improvements of roads and waterways—apparently, without a thought that such agreements might require the explicit, *ex ante* consent of the

---

45 WALLACE R. VAWTER, INTERSTATE COMPACTS—THE FEDERAL INTEREST 6 (1954).

46 *Holmes v. Jennison*, 39 U.S. (14 Pet.) 540, 572 (1840).

47 For an analysis of the "one voice" rationale in *Holmes v. Jennison* and subsequent cases *see* Swaine, *Negotiating Federalism*, 49 DUKE L. J. at 1224-1236.

48 *Holmes v. Jennison*, 39 U.S. (14 Pet.) 540, 572 (1840).

Congress.[49] The understandable desire to facilitate useful cooperative ventures—without subjecting them to the potentially onerous congressional consent requirement—prevented several Justices from joining Taney's opinion in *Holmes v. Jennison.*[50] Over time, it prompted a separation of the foreign from the domestic Compact Clause.[51] The Supreme Court followed Taney on a "one-voice" theory of the foreign Compact Clause[52] and, domestically, drifted toward the position that the Clause applied only to a relatively narrow class of agreements.

The unlikely starting point of the latter development can be found in Justice Joseph Story's attempt, in his influential *Commentaries on the Constitution of the United States*, to distinguish state "treaties," which the Constitution prohibits absolutely, from "agreements and compacts," which are permissible with the consent of Congress. Noting the dearth of contemporaneous evidence that would shed light on the Founders' distinction between treaties (etc.) and agreements (etc.), Story suggested—tentatively, and admittedly on little authority but his own speculation—that the absolute prohibition

---

49 Engdahl, *Interstate Arrangements,* 64 MICH L. REV. at 66.

50 *Id.* at 86.

51 That development parallels both the extra-textual separation of a foreign from a domestic (negative) Commerce Clause and the ostensibly textual but probably mistaken limitation of the Import-Export Clause to foreign rather than interstate trade, *see Woodruff v. Parham*, 75 U.S. (8 Wall.) 123 (1868). (As for "probably mistaken" *see Camps Newfound/Owatonna v. Town of Hamilton*, 520 U.S. 564, 610-40 (1997) (Thomas, J., diss.)) The general trend towards a restrictive view of state authority in matters affecting foreign affairs explains why the "domestic" Compact Clause should be somewhat broader than its foreign cousin. It does not, however, explain the wholesale emasculation of the domestic Compact Clause.

52 *See, e.g.*, *United States v. Rauscher*, 119 U.S. 407, 414 (1886) (suggesting that *Holmes v. Jennison* was based on a general principle of exclusive federal control over foreign relations and endorsing that position).

extends to "treaties of a political character" and the qualified prohibition, to agreements involving the exercise of "what might be deemed mere private rights of sovereignty."[53]

For reasons that will appear shortly,[54] Story's distinction is the wrong starting point for a sensible understanding of the Compact Clause. (The right starting point is the distinction between the logic of the Supremacy Clause on the one hand and the qualified or absolute prohibitions of Article I, Section 10 on the other.) Wholly apart from that consideration, though, the Founders' or Justice Story's distinction (whatever precisely it may have been) does not remotely suggest that some interstate agreements should be *exempt* from the Compact Clause. The Founders, obviously, believed no such thing. Neither did Justice Story—who, tellingly, joined Chief Justice Taney's opinion in *Holmes v. Jennison* and its expansive understanding of "agreements and compacts." Nonetheless, "[i]n a curious feat of judicial doubletalk, Story's distinction between 'treaties' and 'agreements or compacts' was applied to the new task of exempting all but a narrow class of 'agreements and compacts' from the requirement of congressional consent."[55]

That development, ably described by Engdahl,[56] found recognition by the U.S. Supreme Court in *Virginia v. Tennessee*,[57] an 1893 case involving a border dispute between the two states. "By its terms," Justice Field mused for a unanimous Court—alluding to, without citing, Chief Justice Taney's broad interpretation in *Holmes v.*

---

53 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES sec. 1397 (1st ed. 1833) (in subsequent editions, sec. 1403).

54 *Infra* nn. and accompanying text.

55 Engdahl, *Interstate Arrangements* at 66.

56 *Id.* at 86-88.

Jennison—the Compact Clause is "sufficiently comprehensive to embrace all forms of stipulation, written or verbal, and relating to all kinds of subjects."[58] It extends to agreements "to which the United States can have no possible objection or have an interest in interfering with, as well as to those which may tend to increase and build up the political influence of the contracting states, so as to encroach upon or impair the supremacy of the United States or interfere with their rightful management of particular subjects placed under their entire control."[59] Justice Field concluded that the Compact Clause cannot possibly be read to apply to "*any* agreement or compact." "[L]ooking at the object of the constitutional provision" rather than its text, Field determined that the Clause is "directed to the formation of any combination tending to the increase of political power in the States, which may encroach upon or interfere with the just supremacy of the United States."[60] State agreements, Field argued, should be subject to the constitutional requirement of congressional consent only if they threaten to encroach upon the full and free exercise of federal authority.

Justice Field's discourse on the scope of the Compact Clause in *Virginia v. Tennessee* is dictum, since a later part of his opinion holds that Congress had in fact consented to the border agreement between the two states.[61] Later cases, however,

---

57 148 U.S. 503 (1893).

58 *Id.* at 517-18.

59 *Id.* at 518.

60 *Id.* at 519. A slightly different formulation appears *id.* at 517-18 (distinguishing agreements of no interest to the United States from those "which may tend to increase and build up the political influence of the contracting states, so as to encroach upon or impair the supremacy of the United States or interfere with their rightful management of particular subjects placed under their entire control.")

61 *Id.* at 521-22. *See also* Engdahl, *Interstate Arrangements* at 67 and sources cited *id* n. 22 (passages on scope of Compact Clause probably dictum); *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 467

discussed Field's opinion with approval.[62] In the 1970s, Field's dicta became the U.S. Supreme Court's authoritative holding.[63] In that light, two aspects of the opinion bear emphasis.

First, *Virginia v. Tennessee* views the Compact Clause entirely in its vertical, state-to-federal dimension. It is silent on the horizontal effects of state agreements on non-party states and their citizens. The omission marks a shift from the traditional understanding of the Clause. As Chief Justice Taney put it, the point of the Compact Clause is "to guard the rights and interests of the other states, and to prevent any compact or agreement between any two States, which might affect injuriously the interest of the others."[64] It is true that the Clause also, and simultaneously, protects national interests, but the most urgent among those national interests is the protection of comity and equality among the states.[65] It is unlikely that Justice Field intended to devalue that consideration; his failure to mention it, and his language suggesting that the Compact Clause involves the balancing of state versus federal interests, probably flows from the posture and the legal issue of the case. Nonetheless, the shift in emphasis proved fateful and, over time, led to a wholesale judicial indifference to the horizontal concerns that underpin the Compact Clause.[66]

(characterizing those passages as dictum). *But see id.* at 489 (White, diss.) ("*Virginia v. Tennessee* quite clearly holds that not all agreements and compacts must be submitted to the Congress.")(footnote omitted).

62 *See, e.g.*, *North Carolina v. Tennessee*, 235 U.S. 1 (1914); *Stearns v. Minnesota*, 179 U.S. 223 (1900); *Wharton v. Wise*, 153 U.S. 155 (1894). *See also* U.S. Steel v. Multistate Tax Comm'n, 434 U.S. 452, 469 n. 20 (citing state cases relying on the *Virginia v. Tennessee* "test").

63 *Infra* nn. and accompanying text.

64 *Florida v. Georgia*, 17 How. 478, 494 (1855).

65 Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 693-95.

66 *See infra* nn. and accompanying text.

Second, even on the functional grounds urged by Justice Field—that is, wholly apart from textual considerations—the "object" of the Compact Clause warrants no inference to the effect that state agreements that hold no interest for the United States should be exempt from the congressional consent requirement. The institutional question is, who gets to say in the first instance what does or does not constitute an interference with the full and free exercise of federal authority. The constitutional rule, obviously, deprives the states of that authority in all cases. It also deprives the judiciary of an independent role in deciding whether or not state agreements are subject to, or should receive, congressional consent. In sketching the contours of a kind of safe harbor for (presumably) run-of-the-mill state cooperation, *Virginia v. Tennessee* worked a shift both in the appraisal of the risks and dangers of state agreements and in the judiciary's role.

The extent of that shift is not altogether clear. If the requirement of congressional consent is maintained for all state agreements that *might* implicate federal supremacy concerns, the practical effects will be quite similar to those of the blanket constitutional rule.[67] If, on the other hand, the consent requirement is triggered only by state agreements that *demonstrably* encroach upon federal supremacy, the Compact Clause is rendered a virtual nullity: with or without the Clause, such agreements violate the ordinary rules of federal supremacy and preemption. In the 1970s, the U.S. Supreme Court adopted this latter construction.

---

[67] Engdahl, *Interstate Arrangements* at 69, observes that *Virginia v. Tennessee* has in political practice been understood "in terms of the possible, rather than the actual, effects of 'compacts.'" In particular, states have sought congressional consent for compacts where, under a strict reading of the precedents, no consent is required. As noted, however, the states have not always exercised such restraint and deference.

New Hampshire v. Maine (1976),[68] like *Virginia v. Tennessee*, arose over the identification of a pre-existing state boundary line. The principal question was whether the judicial acceptance of an agreement and proposed consent decree between the attorneys general of the two states, without an independent judicial examination, was consistent with the Supreme Court's Article III functions. Having answered that question in the affirmative (over a dissent by three Justices), Justice Brennan's opinion for the Court devoted a slim two paragraphs to New Hampshire's "suggestion" that the acceptance of the consent decree without an independent judicial review might circumvent the Compact Clause. Those paragraphs cite *Virginia v. Tennessee* for the proposition that a state agreement that merely defines a "true and ancient boundary," as distinct from an "alienation of territory," is not an "Agreement or Compact" or at any rate, not a compact of the sort that would require congressional approval.[69]

A brief 20 months after *New Hampshire v. Maine*, the Supreme Court put that decision and *Virginia v. Tennessee* to astonishing use. In sustaining a multistate compact governing the state taxation of business income in interstate commerce, the Court held that no otherwise constitutional state agreement or compact requires congressional approval.

The tax compact at issue in *U.S. Steel Corp. v. Multistate Tax Commission*[70] was formed in the aftermath of the Supreme Court's 1959 decision in *Northwestern States*

---

[68] 426 U.S. 363 (1976).

[69] *New Hampshire v. Maine*, 426 U.S. at 369-370 (quoting *Virginia v. Tennessee*, 148 U.S. 503, 522 (1893)).

[70] 434 U.S. 452 (1978).

Portland Cement Co. v. Minnesota.[71] Under a long line of Supreme Court precedents, a company's income from sales in foreign states constituted income from interstate commerce and could not be taxed in or by those states (so long as the company carried on exclusively interstate business). In *Portland Cement*, the Supreme Court departed from those precedents and held that states could, after all, tax interstate commerce and its proceeds, provided that the taxed entity has some kind of "nexus" to the taxing jurisdiction and the tax is "fairly apportioned" among the states.[72] Corporate America promptly urged Congress to overturn *Portland Cement*. Just as promptly, Congress slapped a nameless moratorium, PL 86-272, on the state taxation of interstate business income of firms whose foreign-state operations did not exceed minimal activities—such as solicitation and delivery—enumerated in the statute.[73] That "safe harbor" moratorium satisfied neither the states nor corporate America.[74] When the world's greatest deliberative body actually got around to deliberating, it proved unable to resolve the interest group conflict. Commissions and committees held lots of hearings and produced reams of paper, but none of the dozen bills introduced over the span of a decade received an up-or-down vote on the floor.[75]

---

71 *Northwestern States Portland Cement Co. v. Minnesota*, consolidated on appeal with Williams & Stockham Valves & Fittings, Inc., 358 U.S. 450 (1959).

72 *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. at 464-65 (1959).

73 "Imposition of net income tax—Minimum standards," P.L. 86-272, 73 Stat. 555, 5 U.S.C. secs. 381 *et seq*. (1959).

74 *See* Jerome R. Hellerstein, *State Taxation Under the Commerce Clause: An Historical Perspective*, 29 VAND. L. REV. 335, 339-340 (1976) (noting that P.L. 86-272 largely immunized small multistate businesses, while leaving national corporations exposed).

75 The strenuous but unsuccessful congressional efforts to reach an accommodation on interstate business taxation in the wake of *Portland Cement* are described in vivid detail in Justice White's dissent in *U.S. Steel*, 434 U.S. at 486-89.

The 1967 Multistate Tax Compact (MTC) established a standing Multistate Tax Commission. The principal purpose of the Commission, which is composed of the tax administrators from all member states, is to facilitate the administration of state taxation for multistate businesses. Specifically, the Compact's stated purposes are to facilitate the proper determination of multistate taxpayers' state and local tax obligations; to promote uniformity; to facilitate taxpayer convenience and compliance; and to avoid duplicative taxation.[76] To that end, the member states endowed the Commission with regulatory authority to determine rules for the allocation and apportionment of business income among member states and other multistate tax issues, subject to the member-states' participation in the proceeding and subsequent approval of the regulations;[77] with executive authority to conduct corporate tax audits, upon request by a member state or *sua sponte*;[78] and with judicial authority to adjudicate disputes, through compulsory arbitration, over the allocation of business income in disputes between taxpayers and member-states' tax authorities.[79] The MTC became effective, in accordance with its terms, upon the formal enactment by the legislatures of seven states.[80] The MTC's

---

[76] Multistate Tax Compact art. I (available at http://www.mtc.gov/ABOUTMTC/compact.htm) (hereafter "MTC").

[77] MTC art. VII, IV.

[78] MTC art. VIII.

[79] MTC art. IX. Due to opposition by the State of California, however, this provision did not go into effect. Jerry Sharpe, *State Taxation of Interstate Businesses and the Multistate Tax Compact: The Search for a Delicate Uniformity*, 11 COLUM. J. LAW & SOC. PROBS. 231, **246 [chk p.]** (1975)

[80] *See* MTC art. X(1).

architects sought congressional approval for their creation, and numerous bills to that effect were introduced in Congress. None of them, however, received formal action.[81]

Business interests sued in state and federal courts, arguing that the MTC violated the Compact Clause because Congress had failed to consent to the arrangement.[82] In *U.S. Steel*, the U.S. Supreme Court decisively rejected that challenge.[83] Writing for a majority of seven Justices, Justice Powell held that the Compact Clause covers only state agreements that may affect federal supremacy. The MTC, according to the Court, posed no such danger.

Having briefly described the MTC's origin and purposes and the fate of the case in the courts below, the *U.S. Steel* majority devoted twelve heavily footnoted pages to discussing the constitutional origins of the Compact Clause and the congressional consent requirement in the Supreme Court's precedents. It described Justice Field's misinterpretation, in *Virginia v. Tennessee*, of Justice Story's *Commentaries* as just that—a misinterpretation;[84] characterized Field's remarks on the limited applicability of the Compact Clause as "an extended dictum";[85] and conceded that subsequent

---

81 Robert M. White, *The Constitutionality of the Multistate Tax Compact*, 29 VAND. L. REV. 453, 461 (1976).

82 *See*, in addition to *U.S. Steel*, *Kinnear v. Hertz Corp*., 545 P.2d 1186 (Wash. 1976) (sustaining interstate joint audit provisions of the Multistate Tax Compact against Compact Clause and other challenges)(discussed in White, *The Constitutionality of the Multistate Tax Compact*, 29 VAND. L. REV. 453 (1976)).

83 In addition, the *U.S. Steel* plaintiffs raised challenges under the Equal Protection, Due Process, and Commerce Clauses. The Supreme Court roundly rejected those claims. *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 478-79.

84 *Id.* at 468 n. 19.

85 *Id.* at 467.

endorsements of that dictum also constituted dicta.[86] The opinion maintained, however, that Field's dictum became an actual holding in *New Hampshire v. Maine*.[87]

Powell's characterization of the precedent is simply false.[88] Had the *New Hampshire* Court meant to endorse a broad proposition that it had theretofore treated as mere dictum, it would presumably have devoted more than two cursory paragraphs to the matter.[89] In point of fact, the *New Hampshire* Court explicitly *declined* to rule on the scope of the Compact Clause and its congressional consent requirement.[90] Wisely, then, Powell rested the remainder of his opinion in *U.S. Steel* precisely not on the purported "holding" of *New Hampshire* but on the dictum of *Virginia v. Tennessee*. He quickly dismissed petitioners' argument that *Virginia v. Tennessee* should be limited to "bilateral agreements involving no independent administrative body."[91] Powell conceded that states and the federal government had always thought compacts of comparable complexity and consequence to require congressional consent, but dismissed that fact as a political

---

86 *Id.* at 459; 470 (noting that none of the cases citing Justice Field's test with approval explicitly applied it).

87 *Id.* at 460.

88 Powell probably knew it to be so. His claim that *New Hampshire v. Maine* constitutes a binding endorsement of *Virginia v. Tennessee*'s dicta appears at the beginning, not the end, of his *U.S. Steel* disquisition on the history of the Compact Clause. Had *New Hampshire* in fact established a binding precedent, in so recent a case, that entire discussion would have been redundant.

89 Certainly, the two dissenting Justices in *U.S. Steel* would have caught the point in *New Hampshire*. They did in fact dissent in that earlier case—without, however, even remarking on the congressional consent requirement and its interpretation in *Virginia v. Tennessee*.

90 *New Hampshire v. Maine*, 426 U.S. at 366 (having sustained Maine's exception to rejection of proposed consent decree, on the grounds that entry is consistent with Article III, Court has "no occasion to address the other exceptions filed by the States.") Those "other exceptions" cover New Hampshire's "suggestion," *id.* at 369, that the Compact Clause might bar the consent decree.

91 *Id.* at 471.

practice without precedential value.[92] He then proclaimed Justice Field's position, which he had earlier described as both misguided and dictum, as the "*Virginia v. Tennessee* rule"[93] and—without mentioning *New Hampshire v. Maine*—applied that so-called rule to the MTC.

In light of the manifest differences between the border-fixing agreement in *Virginia v. Tennessee* and the convoluted tax regime at issue in *U.S. Steel*, one ought to be skeptical about distilling Justice Field's musings into a mechanical "rule" that limits the application of the Compact Clause to arrangements that might compromise federal supremacy. Since a border demarcation between two contiguous states is unlikely to involve the interests of a third state, Justice's Field's preoccupation with the vertical effect of compacts was, as noted, understandable, even though lamentable. In contrast, the application of that one-dimensional rule to the MTC—a regulatory regime that very obviously involves the interests of sister-states—effectively excludes the protection of those interests, once thought to be a principal purpose of the Compact Clause, from its reach. As Justice White observed in dissent, it was "obvious that non-Compact States can be placed at a competitive disadvantage by the Multistate Tax Compact."[94] Not bothering to deny the fact, the majority responded that states are similarly affected by any number of policies enacted by individual sister states.[95] The gross theoretical mistake behind this

---

92 *Id.* n. 24.

93 *Id.* at 472.

94 *Id.* at 495.

95 *Id.* at 477-78..

averment is discussed below.[96] Suffice it here to state the readiest reply: so what? Those other state policies are not constitutionally disfavored. State compacts are.

Having effectively excluded the MTC's horizontal effects on sister-states from constitutional considerations, the *U.S. Steel* majority proceeded to minimize the impact of the arrangement on federal supremacy. [T]he pertinent inquiry" under *the Virginia v. Tennessee* "rule," the *U.S. Steel* Court observed in professed agreement with the petitioners' position, "is one of potential, rather than actual, impact upon federal supremacy."[97] But that is not the test the *U.S. Steel* Court actually applied. Of the MTC's *potential* impact, an abundance of evidence was before the Court. Much of it found its way into Justice White's dissent, which describes the protracted federal debate preceding and accompanying the creation of the MTC; the MTC's explicit organizational purpose to forestall federal tax legislation; and the sustained, serious political disputes between the MTC and the federal branches over international treaties affecting the taxation of income earned by foreign companies in the United States.[98] In light of the "hostile stalemate" between the MTC and the federal government, Justice White concluded, the MTC's potential impact on federal concerns was simply beyond peradventure.[99]

The *U.S. Steel* majority's response to these observations appears in the following passage:

---

96 *Infra* nn. and accompanying text.

97 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 472. The dissenting Justices commended the majority opinion on that recognition, and couched the disagreement as merely a question of applying the "potential impact" standard to the MTC. *Id.* at 484. The concession is unwarranted.

98 *Id.* at 486-88. *See also infra* nn. and accompanying text.

99 *Id.* at 488.

> "*On its face the Multistate Tax Compact contains no provisions* that would enhance the political power of the member States in a way that encroaches upon the supremacy of the United States. There well may be some incremental increase in the bargaining power of the member States quoad the corporations subject to their respective taxing jurisdictions…. But the test is whether the Compact enhances state power quoad the National Government. *This pact does not purport to authorize the member States to exercise any powers they could not exercise in its absence.* Nor is there any delegation of sovereign power to the Commission; each State retains complete freedom to adopt or reject the rules and regulations of the Commission. Moreover, … , each State is free to withdraw at any time." [100]

Putting aside, for now, the highly questionable characterization of the MTC,[101] the italicized introductory phrase shows that the majority's test is not the "potential impact" rule of *Virginia v. Tennessee*; the test is an *actual* conflict between the language of some compact provision and a federal (constitutional or statutory) norm.[102] Consistent with this reading, the passage just quoted repeatedly formulates the "pertinent inquiry" as a question of affirmative, rather than potential, "enhancement" and "encroachment." Under that theory, no state compact requires congressional approval unless it declares an invasion of federal supremacy *in haec verba*—on its face, as it were.

---

100 *Id.* at 472-73 (emphasis added).

101 *See infra* nn. & accompanying text.

102 A true "potential impact" cannot distinguish between the "facial" and "as-applied" validity of a contested provision. A discussion of this or that application and operation of the provision—along the lines of Justice White's *U.S. Steel* dissent—is simply an affirmative showing that the provision has, or has already had, the forbidden potential. That showing is not a basis for a separate "as-applied" challenge; it goes directly to the validity of the provision. The *U.S. Steel* Court ignored this logic. Throughout its opinion, the majority deflected the petitioners' and the dissenters' arguments about the operation of the Compact with references to the MTC's purportedly unobjectionable language. Justice Powell, the author of *U.S. Steel*, in a later case described his opinion as having upheld the MTC against a *facial* challenge: *ASARCO v. Idaho State Tax Comm'n*, 458 U.S. 307, 312 n. 7 (1982). The suggestion that there could be a meaningful distinction between an as-applied and a facial challenge to the MTC—and certainly the veiled suggestion that the former might have succeeded where the latter did not—illustrates that the *U.S. Steel* Court did not simply mis-apply the "potential impact" test; it applied a different test altogether.

The same conclusion flows from the just-quoted contention that the MTC did not "authorize the member States to exercise any powers they could not exercise in its absence," which forms the majority's principal defense of its ruling. Individual states may of course legislate in areas of concurrent authority, including especially interstate commerce (within the bounds of the dormant Commerce Clause), until Congress stops and preempts them. Therefore, the *U.S. Steel* Court concluded, they may do so collectively and by compact. As Justice White pointed out, however, that conclusion cannot be right. "The [Compact] Clause must mean that some actions which would be permissible for individual States to undertake are not permissible for a group of States to *agree* to undertake."[103] Otherwise, the Clause is empty.

The majority's curt reply to this objection is that it confuses federal *interests* with federal *supremacy*. The MTC plainly governs the taxation of interstate commerce, which the Constitution commits to the care and authority of the United States Congress. However, "every state cooperative action touching interstate or foreign commerce implicates some federal interest. Were that the test under the Compact Clause, virtually all interstate agreements and reciprocal legislation would require congressional approval."[104] That, of course, is what the text of the Compact Clause provides. We know, however, that not *all* interstate agreements can sensibly be viewed as requiring congressional approval; *vide Virginia v. Tennessee*. Therefore, *none* should require approval save those that, "on their face," purport to exercise a power reserved exclusively

---

[103] *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 482 (emph. in the original).

[104] *Id.* at 479 n. 33.

to the federal government and those that conflict with a preemptive federal law. That syllogism is the sum and substance of contemporary Compact Clause doctrine.

III. Constitutional Logic

After *U.S. Steel*, it is impossible to imagine a state compact that would run afoul of the Compact Clause without first, or at least also, running afoul of other, independent constitutional obstacles. But while *U.S. Steel* effectively declared the Compact Clause inoperative, it is the *only* Supreme Court decision in over two centuries to so hold. No case prior to *U.S. Steel* embodied such a holding, and while the Supreme Court has never questioned the *U.S. Steel* decision, it has never affirmatively relied on it, either.[105] Thus,

---

[105] Supreme Court decisions contain the following citations to *U.S. Steel Corp. v. Multistate Tax Comm'n*: *Hess v. Port Auth. Trans-Hudson Corp*., 513 U.S. 30, 57 (1994) (diss); *F.W. Woolworth Co. v. Taxation & Revenue Dept*., 458 U.S. 354, 357 (1982); *ASARCO, Inc. v. Idaho State Tax Comm.*, 458 U.S. 307, 310, 312 (1982); *Western & Southern Life Ins. Co. v. State Bd. Of Equalization*, 451 U.S. 648, 671 (1981); *Cuyler v. Adams*, 449 U.S. 433, 440; 449 U.S. at 451 (diss.) (1981); *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 439 (1980); *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 282 (diss.) (1978). None of these cases relies on the *U.S. Steel* holding concerning the congressional consent requirement; only two even mention it. The first is Justice Rehnquist's dissent in *Cuyler v. Adams*, 449 U.S. 433, 451 (1981). The second, *Hess v. Port Auth. Trans-Hudson Corp*., 513 U.S. 30, 40 n. 10 (1994) contains a throw-away footnote that says, without explicitly holding, that "federal consent is not required" for compacts that do not implicate federal concerns; the note cites *Virginia v. Tennessee*, 148 U.S. 503, 517-520 (1893) but, inexplicably, *not U.S. Steel* for the proposition.

The only case that can be construed as an explicit affirmation of U.S. Steel is the cavalierly reasoned decision and opinion in *Northeast Bancorp v. Bd of Governors of Fed. Reserve Sys*., 472 U.S. 159 (1985). The so-called Douglas Amendment to the Bank Holding Company Act of 1956 permitted the Federal Reserve Board to approve bank applications to purchase a bank in another state if, and only if, the acquisition was "specifically authorized by the statute laws of the [acquisition target's] State." 12 U.S.C. 1842(d). Several New England states authorized acquisitions by banks headquartered in other New England states, provided those states enacted a reciprocal authorization (though not necessarily one limited to New England states). New York banks argued that the reciprocal statutes permitting acquisitions by out-of-state New England banks, *but not* by banks outside that region, violated, *inter alia*, the dormant Commerce Clause and the Compact Clause. The Supreme Court determined that the Douglas Amendment authorized the arrangement, which would otherwise have constituted a violation of the dormant Commerce Clause. As to the Compact Clause claim, Chief Justice Rehnquist expressed "some doubt as to whether there is an agreement amounting to a compact." *Northeast Bancorp*, 472 U.S. at 175. Finding "several of the classic indicia of a compact" missing, *id*., the Court construed the challenged state laws—correctly, to my mind—as a reciprocity agreement rather than a compact. However, continued the Court, "even if we were to assume" the existence of a compact, not all compacts require approval. The petitioners' contention that the

unlike constitutional questions that are effectively immunized from principled consideration by piles of precedents, the Compact Clause affords us the luxury of being able to take a single step back to the actual Constitution and its logic.

At first impression, that endeavor appears unpromising. Constitutional scholars from Justice Story on forward have noted the dearth of contemporaneous evidence on the specific meaning of the Compact Clause. "The records of the Constitutional Convention furnish no light as to the source and scope" of the Clause.[106] Its only mention in the *Federalist Papers* appears in No. 44, written by James Madison. The prohibition against treaties, alliances, and confederations, Madison writes, was "copied" from the Articles of Confederation into the Constitution, "for reasons which need no explanation."[107] The restraint on state imposts and duties "is enforced by all the arguments that prove the necessity of submitting the regulation of trade to the federal councils,"[108] and the qualified prohibitions of the third paragraph (which include the Compact Clause) "fall

---

alleged regional compact affronted the sovereignty of sister-states outside New England was baseless: "We do not see how the statutes in question either enhance the *political* power of the New England States at the expense of other states or have an 'impact on our federal structure.'" *Northeast Bancorp*, 472 U.S. at 176 (quoting and citing *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 471, 473)(emph. in original).

On one reading (*see* LAWRENCE H. TRIBE, 1 AMERICAN CONSTITUTIONAL LAW 1245 & *id.* n. 40 (3rd ed. 2000), *Northeast Bancorp* stands for the following proposition: an economic "Fortress New England," to the exclusion of other states, violates (barring congressional authorization) the judge-made dormant Commerce Clause *but not* the Compact Clause, *because it has no impact on the federal structure*. Respectfully, the assertion—unsupported in *Northeast Bancorp* by any further argument or explanation—would have floored the Founders. Contemporary European leaders would likewise be astounded to learn that their internal market arrangements have no political and institutional import. *See infra* n.

It is perfectly plausible, and far more charitable, to read the *Northeast Bancorp* Court's pronouncements following the "even if" sentence as dicta. On that reading, the case holds that reciprocity agreements—as distinct from compacts—do not require congressional approval. That proposition is defensible, though not self-evidently or necessarily correct; *see infra* nn. and accompanying text. On the yet more difficult question of *selective* reciprocity agreements in *Northeast Bancorp* and in general *see infra* n.

106 Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 694 (1925).

107 FEDERALIST PAPERS No. 44 (Madison), 281 (Clinton Rossiter ed. 1961).

108 *Id.* at 283.

within reasonings which are either so obvious, or have been so fully developed, that they may be passed over without remark."[109] And to all a good night. No record exists on the distinction between treaties and compacts. Some scholars have argued that the Founders derived it from then-extant theories and concepts developed by leading authorities on the Law of Nations, especially Vattel.[110] But if so, their understanding was lost even to the immediately following generation.[111]

The interpretive fog, however, is almost entirely a result of the misguided preoccupation with the distinction between treaties and compacts, between absolute and qualified prohibition. The distinction that preoccupied the Founders was the far more basic choice between two very different institutional means of federal control over centrifugal tendencies in the states—legal supremacy, and a (qualified or absolute) prohibition. On *that* fundamental choice, the historical record is as clear as sunlight. The adoption of a qualified prohibition, in lieu of a plain-vanilla supremacy arrangement, for state agreements is the key to the constitutional logic of the Compact Clause.

---

109 *Id.*

110 *See especially* the erudite discussion by Engdahl*, Interstate Arrangements* at 75-81.

111 Chief Justice Marshall, for a prominent example, used the terms "compacts" and "treaties" interchangeably: "A state is forbidden to enter into any treaty, alliance or confederation. If these *compacts* are with foreign nations, they interfere with the treaty-making power, which is conferred entirely on the general government; if with each other, for political purposes, they can scarcely fail to interfere with the general purpose and intent of the constitution." *Barron v. Mayor & City Council of Baltimore*, 32 U.S. (7 Pet.) 243, 249 (1833) (emphasis added).

A. Congressional Consent and Supremacy

James Madison arrived at the Convention loaded for bear. The linchpin of his agenda was a national "negative" on state laws,[112] which should apply "in all cases whatsoever."[113] What Madison had in mind was not a federal veto over existing state legislation—a kind of *ex post* federal preemption. Rather, in advocating a negative apply "in all cases whatsoever," he insisted that no state law should go into effect without federal approval.[114] Madison intended to arm the national government with the means to stem centrifugal and aggressive tendencies in the states—their proclivity "to invade the national jurisdiction, to violate treaties and the law of nations & to harass each other with rival and spiteful measures dictated by mistaken views of interest."[115] As the broad sweep of his proposal suggests, though, Madison also desired to protect the citizens of the various states from depredations *by their own state governments*. The Convention, Madison argued, should "seize the occasion of reforming the national government to treat the internal defects of the states."[116] The reason for Madison's vast ambition—seemingly absurd, considering that the Convention had more than its work cut out in establishing a viable Union—was his conviction that the states' outward aggression and their internal

---

[112] Larry D. Kramer, *Madison's Audience*, 112 HARV. L. REV. 611, 634-35 and sources cited *id*. nn. 101, 102 (1999) (describing negative as the central element of Madison's plans).

[113] Letter from James Madison to Thomas Jefferson (Mar. 19, 1787), in 9 THE PAPERS OF MADISON 318, 318 (Robert A. Rutland et al. eds., 1975) (hereafter PAPERS OF MADISON).

[114] Charles F. Hobson, *The Negative on State Laws: James Madison, the Constitution, and the Crisis of Republican Government*, 36 WM. & MARY QUART. (3rd ser.) 215, 219 (1979).

[115] Letter from James Madison to George Washington (Apr.16, 1787), in 9 PAPERS OF MADISON 382, 384. Kramer, *supra* n. at 626-636, provides an excellent account of the genesis of Madison's views on the negative and its intended purposes and scope.

[116] Kramer *supra* n. xxx at 634 n. 99 (quoting Jack N. Rakove, ORIGINAL MEANINGS: POLITICS AND IDEAS IN THE MAKING OF THE CONSTITUTION 47 (1996)).

defects had a common source: factionalism. In pressing for a comprehensive negative, Madison proposed to tackle that problem at the source, as opposed to curbing its particular, outward manifestations.[117]

The Convention debated Madison's negative, in somewhat different versions, on three occasions: in early June, in the first run-through of the Virginia delegation's plan for the Convention; in mid-July, when Madison's proposal got entangled in the debate over the Great Compromise on representation in the federal legislature and sidetracked by Hamilton's notorious diatribe on the glories of the British system; and again in August, when Madison, with an obduracy born of despair over the fate of the nation, re-introduced the proposal to an impatient Convention that had long moved on to constitutional minutiae.[118] On all three occasions, Madison's proposal for a blanket negative was rejected. Two arguments carried the day against Madison. First, his numerous opponents denounced the proposed negative as a nationalistic instrument that would (as Governor Morris put it) "disgust all the States,"[119] thus dooming the constitutional venture.[120] Second, the proposed negative would sweep too broadly,

---

117 *Id.* at 648 *et pass*. The Convention, of course, rejected Madison's proposal and instead subjected particular classes of state laws (compacts, duties, etc.)—those with obvious deleterious effects on sister-states—to particularized prohibitions and negatives into the Constitution. Kramer argues that the delegates never grasped Madison's point that those odious measures merely illustrated the general problem of state factionalism. For the purposes at hand, nothing hangs on the question of whether the delegates failed to grasp Madison's argument or whether they understood and rejected it. Either way, the Convention clearly apprehended the dangers that certain classes of state laws would pose to the harmony of the union.

118 Kramer, *supra* n. at 650.

119 2 THE RECORDS OF THE FEDERAL CONVENTION of 1787, 28 (Madison's notes, July 17, 1787) (Max Farrand ed., rev. ed. 1937)[hereafter RECORDS OF THE FEDERAL CONVENTION].

120 2 RECORDS OF THE FEDERAL CONVENTION 391 ("Mr. Rutlidge. 'If nothing else, this alone would damn and ought to damn the Constitution. Will any State ever agree to be bound hand & foot in this manner.'") (Madison's notes, Aug. 23, 1787).

rendering it both impracticable and unnecessary. The negative would compel states to obtain national consent for urgent matters, when the national legislature might not be in session. At the same time, the negative would compel Congress to concern itself with the states' "internal police," and thus with state activities "to which the United States can have no possible objection or have an interest in interfering with," as Justice Field would later put it.[121]

The Convention rejected Madison's proposal for an all-encompassing negative and instead adopted federal supremacy—asserted either through the courts, in the ordinary course of deciding cases and controversies, or through congressional legislation—as the general constitutional arrangement. Strictly speaking, the negative and federal supremacy are not mutually exclusive alternatives. States may seek to evade a negative, or for that matter, an absolute prohibition, just as they may seek to evade an ordinary federal statute. On way or the other, federal supremacy depends on judicial enforcement. (Hamilton, in fact, in defending the need for federal supremacy and the prominent role of the courts in its enforcement, illustrated his point by stressing the near-certainty of state violations of absolute and qualified constitutional prohibitions, rather than state interferences with, say, the federal regulation of interstate commerce.)[122] The difference is the default principle on which federal supremacy operates: whereas the negative renders state laws inoperative, pending affirmative congressional action, the supremacy principle alone—let's call it "mere supremacy"—permits state law to be enacted and to remain in effect until and unless a court or the Congress sets them aside.

---

[121] Hobson, *supra* n. at 227 (citing and summarizing the delegates' practical objections). *Cf.* Justice Field's formulation in *Virginia v. Tennessee*, 148 U.S. at 518 (1893).

[122] FEDERALIST PAPERS No. 80, at 475 (Hamilton).

In that sense, the negative and mere supremacy *are* mutually exclusive alternatives. The Convention clearly understood them as such, and the adoption of the Supremacy Clause promptly followed the rejection of the negative.[123]

However, the Convention retained absolute prohibitions *or a congressional negative* for certain classes of state laws—those that are now listed in Article I, Section 10, including the Compact Clause. The congressional consent requirement for state agreements and compacts is the Madisonian negative, in a specified range of application. This decision was not some quid pro quo to appease the ornery Madison. Rather, even as the delegates rejected Madison's entreaties to use the Convention as an opportunity to reform state politics (preferring instead to leave that project for another time and place),[124] they emphatically agreed with his contention that certain species of state laws—the "rage" for paper money, debtor relief laws, import duties—posed alarming dangers to sister-states and, hence, to the union. For these classes of state laws, including compacts, the Convention deliberately broke with mere supremacy and instead adopted either an absolute prohibition or the "disgusting" negative. Uniformly, the prohibitions and negatives are directed against classes of state laws with a manifest detrimental effect on sister-states, and hence the harmony of the Union. As Madison, who viewed those laws (along with the states' internal defects) as an outgrowth of unchecked factionalism, might have put it, the Convention sought to arrest factionalism at the borders.

---

123 Hobson, *supra* n. xxx at 228. As for "clearly understood," see, *e.g.*, Gov. Morris's comment immediately preceding the rejection of the negative proposal on July 17 ("Mr. Govr. Morris was more & more opposed to the negative. The proposal of it would disgust all the States. A law that ought to be negatived will be set aside by the Judiciary departmt. and if that security should fail; may be repealed by a Nationl. Law." 2 RECORDS OF THE FEDERAL CONVENTION 28 (Madison's notes).

124 Kramer, *supra* n. at 647-48.

Before pursuing the logic of this constitutional choice, two points—one minor, the other of some significance—merit a brief mention. First, the nature of the congressional consent clauses in Article I, Section 10 sheds light on Madison's cursory discussion of those provisions, including and especially the Compact Clause, in the *Federalist Papers*.[125] While Madison may have genuinely believed that the dangers of state compacts were "too obvious" to warrant discussion, and while he may have expected his audience to share that view, his extreme brevity may also reflect an effort to deflect unwanted (Antifederalist) attention from the distinctly nationalistic resolution of the compact problem in the Constitution.[126] Having experienced the determined opposition to the general negative at the Convention, the Madison of the *Federalist Papers* was hardly inclined to boast that his "pet scheme"[127] was actually retained for certain classes of state laws.

The second, more consequential point concerns the fateful debate over the distinction between absolutely prohibited "treaties" (etc.) and "agreements and compacts," which are subject to the Madisonian negative. Putting aside its absurd turns, that debate misses the point that the constitutional choice between absolute and qualified prohibition is secondary, both logically and in terms of institutional significance, to the constitutional choice between federal legal supremacy and (qualified or absolute) prohibition. The distinction between treaties and compacts is of little practical import so

---

125 *See supra* nn. and accompanying text.

126 That interpretation is supported by a telling "mistake" in Madison's account in the *Federalist Papers*: contrary to his representation (quoted *supra* in the text accompanying n.), the constitutional injunction against state treaties was not in fact "copied" from the Articles of Confederation but rather strengthened. "[T]he prohibition in the Articles was conditional; in the Constitution it is absolute." Engdahl, *Interstate Arrangements,* 64 MICH. L. REV. at 75 n. 59.

127 Rakove, *supra* n. at 435.

long as, and because, *neither kind of bargain can be concluded without the approval of Congress*.[128] Congress might mis-classify a compact as a treaty and declare itself constitutionally barred from approving it. That mistake is tantamount to a simple rejection of a compact, and thus without consequence. Conversely, Congress might mis-classify a treaty as a compact and proceed to approve it. That is conceivable, but highly unlikely. The question has never arisen in an actual case and, in light of its unequivocal commitment to the Congress, is quite probably non-justiciable.[129] In any event, a judicial ruling to the effect that Congress mistakenly approved a constitutionally prohibited state treaty would afford more rather than less protection against divisive state agreements.

The distinction between treaties and compacts is not altogether irrelevant. Legislative deliberations on the point should be informed by the Founders' understanding of the constitutional distinction, obscure though it may be.[130] But one should not search

---

[128] Cf. Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 694-95 (identifying constitutional commitment to Congress as the central feature of the Compact Clause).

[129] GATT Implementing Legislation: Hearings on S. 2467 Before the Senate Comm. On Commerce, Science and Transportation, 103rd Cong., 2nd Sess. 285, 319 (hereafter *GATT Hearings*) (Testimony by Lawrence H. Tribe) (suggesting that the classification of particular international agreements as Article II "treaties" or something else may not be justiciable and characterizing the question as "tough"). The case against justiciability is even stronger under Article I, which clearly commits treaties *and* compacts to Congress (regardless of where the distinction is drawn), than under Article II, which provides for the approval of "treaties" without specifying how and by whom they are to be distinguished from other sorts of agreements.

[130] To my mind the most natural interpretation is that treaties (and the like) are something more formal, lasting, and consequential than mere "agreements and compacts." In particular, treaties (and the like) threaten to compromise the parties' sovereignty to a greater extent than mere one-shot agreements. Lawrence H. Tribe, *Taking Text and Structure Seriously: Reflections on Free-Form Method in Constitutional Interpretation*, 108 HARV. L. REV. 1221, 1266-68 and sources cited *id.* (1995). At some point, state agreements may effect such a departure from the original constitutional design that even Congress may not permit them. This view of a constitutional continuum is buttressed by the progression from the less to the more formal within each clause ("Treaties, Alliances and Confederations;" "Agreements and Compacts"). *GATT Hearings, supra* n. at 288 (letter from Prof. Anne-Marie Slaughter submitted into the record by Lawrence Tribe). Assuming that the word "treaty" means the same in Article II as it does in Article I, the Treaty Clause of Article II Sec. 2 Cl. 2, requiring the concurrence of two-thirds of the Senate to treaties made by the President, further supports the interpretation of the text. While that Clause (unlike Article I) does not explicitly distinguish between treaties and other kinds of agreements, the

for a hard-and-fast rule where some play in the joints can easily be tolerated, and may in fact be preferable. The purpose of precluding divisive state agreements has been accomplished, so far as possible, once any and all state agreements have been exempted from mere supremacy and instead been subjected to a negative, or an absolute prohibition. No serious institutional risk or consequence attends to an erroneous congressional identification of a compact as a treaty, or vice versa.

It was only in August, *after* the Convention had made the basic choice on supremacy (in the general run of cases), that the delegates turned to the question of whether the exceptions to that rule should be governed by a negative or an absolute prohibition. Considering the delegates' discussion of the parallel provisions of Article I, Section 10, it may be just as well that the record at this point falls silent on the Founders' Compact Clause. For example, the delegates engaged in a rambling discussion on the distinction, if any, between duties and imposts.[131] The Import Clause eventually came to contain an exception for state charges that are "absolutely necessary" to carry out a state's inspection laws; a parallel qualification for the Tonnage Clause was introduced and discussed (on the day of the Convention's adjournment, and to Madison's obvious irritation), but voted down.[132] The discussions accompanying those choices have an air of pedantry, impatience, and sheer exhaustion. A learned disquisition on the niceties of "compacts" and "treaties" under the Law of Nations, one feels, might well have earned its

---

idea of subjecting treaties, but not (unspecified) other agreements, to a requirement of approval by two-thirds of the Senate makes sense only on the assumption that treaties are something more formal, something more threatening to state and popular sovereignty, than other sorts of arrangements. *GATT Hearings* at 287-88 (Letter from Anne-Marie Slaughter).

131 2 RECORDS OF THE FEDERAL CONVENTION 305-08 (Aug. 16) (Madison's notes).

132 2 RECORDS OF THE FEDERAL CONVENTION 625 (Sept. 15) (Madison's notes).

author a public flogging—and a deserved one at that: the crucial decision against mere supremacy had long been made.

B. Why Mere Supremacy Is Not Enough

The fact that the very same delegates who so resolutely rejected the Madisonian negative deliberately adopted that instrument for state agreements and compacts should carry some constitutional weight. In light of the modern Supreme Court's obtuseness on the point, the reasons for the Convention's decision warrant further exploration.

The most obvious reason has already been suggested: if one rejects, along with the great majority of delegates, Madison's endeavor to remedy the internal defects of state politics at and through the Constitutional Convention, then a general negative is grossly overinclusive. It covers a vast array of state activities that pose no risk to the Union, at considerable institutional cost. As Thomas Jefferson tweaked Madison in a pre-Convention letter from Paris, the proposal "mend[s] a small hole by covering the whole garment."[133] Time and again, Madison's opponents at the Convention turned to this argument. As one Convention delegate (George Mason) put it—again, foreshadowing Field's language in *Virginia v. Tennessee*—it would be highly impracticable and onerous to obtain congressional consent every time a state decides to build a bridge within its own territory.[134]

The overinclusiveness argument obviously does not apply to the use of the negative in areas of state activity that constitute, by broad agreement, manifest threats to

---

[133] Letter from Thomas Jefferson to James Madison (June 20, 1787), in 10 PAPERS OF MADISON 64.

[134] 2 RECORDS OF THE FEDERAL CONVENTION 390 (Madison's Notes).

sister-states and to the union. That observation does not quite explain, though, why the negative is *necessary* in those areas—in other words, why the ordinary exercise of legal supremacy, through the courts or by Congress, is not enough. The answer lies in a comparative analysis of institutional risks and benefits.

Supremacy, in the area of enumerated congressional powers, is plenary, but its exercise is somewhat uncertain. Supremacy must be asserted by courts, in the ordinary course of deciding cases and controversies. Cases may materialize late, or never, and courts may neglect to enforce the rightful supremacy concerns of the United States.[135] Congress can, within its enumerated powers, preempt state legislation and correct errors by displacing inconvenient state laws and (sub-constitutional) judicial decisions, but—to anticipate a point that will shortly emerge as the central justification for the negative—it may not always muster the will or the energy to do so. Supremacy, in short, will produce a number of "false negatives"—that is, unredressed offenses against national rights and prerogatives.

---

[135] *See* 2 RECORDS OF THE FEDERAL CONVENTION 27 (Madison). *See also* Kramer, *supra* n. at 653 n. 180 (discussing Madison's sentiment and citing non-Convention sources). It bears emphasis that "courts," to the Founders, principally meant *state* courts, subject to Supreme Court review. The very real possibility that parochial judicial interpretations of compacts might create strife rather than harmony among the states is an additional reason against reliance on plain-vanilla supremacy in the compact context. In the 20th century, that possibility prompted the Supreme Court to characterize compact law, first, as some kind of "law of the Union" and, later, as unequivocally federal law. *See Delaware River Joint Toll Bridge Comm'n v. Colburn*, 310 U.S. 419 (1940) (approved compact constitutes federal law); *Dyer v. Sims*, 341 U.S. 22 (1950) (state court interpretation of state Constitution in conflict with compact presents federal question;) *Petty v. Tennessee-Missouri Bridge Comm'n*, 359 U.S. 275 (1959) (federal law governs interpretations of compacts); *Cuyler v. Adams*, 449 U.S. 433 (1981) (congressionally approved compacts present federal question regardless of parties' understanding of compact terms); *New Jersey v. New York*, 523 U.S. 767, 782 (1998) (federal courts not bound by state court interpretation of compact). The broad extension of federal law and jurisdiction has problems of its own and has been widely criticized. *See, e.g.*, Note, *Charting No Man's Land: Applying Jurisdictional and Choice of Law Doctrines to Interstate Compacts*, 111 HARV. L. REV. 1991(1998); Note (L. Mark Eichhorn), Cuyler v. Adams *and the Characterization of Compact Law*, 77 VA. L. REV. 1387 (1991); David E. Engdahl, *Construction of Interstate Compacts—A Questionable Federal Question*, 51 VA. L. REV. **xxx** (1965). *See also Petty v. Tennessee-Missouri Bridge Comm'n*, 359 U.S. 275, 283 (1959) (Frankfurter, J., diss*.); Cuyler v. Adams*, 449 U.S. 433, 450 (1981) (Rehnquist, J., diss.).

Those institutional mistakes, however, are tolerable in the general run of cases where inconvenient state laws might call for federal intervention.[136] The institutional alternative would generate an unacceptable number of false positives and, moreover, unacceptable institutional transaction costs. That, in a nutshell, was the case against the general negative. The analysis flips, however, when we have good grounds to suspect that a particular class of state activities spells trouble. Under that scenario, the supremacy arrangement would produce huge error costs, whereas the negative would produce few false positives. Consider the most obvious example, the exercise of concurrent state authority within the ambit of the Commerce Clause. We know that states are perfectly capable of enacting, under that umbrella, protectionist measures disguised as "police power" regulation. Such menaces to sister-states and the Union, however, are relatively rare compared to the great mass of police power regulation. Under the supremacy arrangement of the Commerce Clause, we permit those incursions—pending judicial or congressional intervention—because the costs of subjecting *all* state legislation to congressional preapproval are unacceptably high. Not so, however, with state duties on tonnage or import tariffs. While these measures, too, fall under the general description of "interstate commerce"—and therefore, barring special constitutional treatment, under the operation of the supremacy principle—they can hardly be anything *but* protectionism. Hence, the Constitution subjects them to the negative.

---

136 The paragraph in the text explicates the constitutional choice, not Madison's position. Madison himself believed—based on his experience in the Virginia Assembly—that the typical state legislature "enacted scores of laws, of which a few had genuine merit but the rest were either inconsequential or positively harmful." Hobson, *supra* n. , at 224. The assumption that state legislatures churn out mostly garbage might well warrant a comprehensive negative, so long as it can be provided at reasonable cost. For reasons noted, though, the Convention rejected Madison's proposal.

While even a negative (or for that matter an unqualified prohibition on state laws) cannot entirely preclude evasive state maneuvers, it does provide an added safeguard. The evasion of an unequivocal negative by state legislatures or judges requires more cleverness, factious spirit, and willfulness than does the ordinary "police power" interference with interstate commerce. A state legislature that violates the Import-Export Clause—or the Compact Clause, as written—is unlikely to have done so inadvertently; it should be presumed to have pushed the constitutional envelope. Likewise, a negative or absolute prohibition disciplines courts, so far as possible. The sorting of competing state and federal powers in areas of concurrent authority is a difficult task, and judicial mistakes will be common. Misinterpreting a constitutional injunction against state duties of tonnage or, for that matter, against *any* unapproved state agreement requires willfulness or massive intellectual confusion.[137]

The greatest and central difference between the negative and mere supremacy, however, lies in the federal legislative dynamics. The failure of Congress to assert federal supremacy in all or at least most instances where that might be needed is a matter of institutional design, rather than an occasional lack of will. The constitutional cure, famously described in Madison's *Federalist* No. 51, to the dangers of factionalism is to extend the sphere within which factions must operate and to further hamper their operation, in that extended sphere, through the separation of powers and elaborate supermajoritian safeguards—prominently, in the form of bicameral consent and a presidential veto. These ingenious precautions are worth having—even at the price of

[137] Moreover, an explicit constitutional prohibition (qualified or absolute) will suppress a broad range of state activities that would otherwise become the stuff of litigation. Marginal cases and judicial misinterpretations will occur under any rule; what matters in choosing and evaluating the legal rules is the stuff that never makes it into court.

sacrificing some good laws[138]--so long as the task at hand lies, as mostly it does, in preventing federal legislation from interfering with beneficial or at least harmless activities. (Private orderings are the classic example: whatever occasional market failures such arrangements might produce, they are bound to pale in comparison to the horrors of an institutional system that facilitates interest-group driven government intervention.) The precautions fail, however, and in fact have the opposite of the intended effect, when the objects of federal legislation spell trouble and energetic affirmative action is called for—for instance, because partial legislation at the state level endangers the interests of sister-states. Put more directly, the constitutional obstacles that prevent partial laws at the federal level will, under a mere supremacy arrangement, hamper the national government's ability to redress piggishness at the state level.

The constitutional solution we have inherited is to invert the default rule for problematic classes of state laws. Mere supremacy must rely on the ability of the political branches to stitch together a supermajority in defense of national interests. With respect to the great mass of state legislation, that arrangement will (hopefully) minimize institutional error on either side.[139] The negative, in contrast, compels the *advocates* of proposed state legislation, rather than their opponents, to find the requisite

---

[138] The necessity of safeguarding against partial legislation is of course the central defense of bicameralism and the presidential veto in the FEDERALIST PAPERS. *See, e.g.*, Hamilton's defense of the presidential veto as a safeguard against "the mischief of that inconstancy and mutability in the laws, which form the greatest blemish in the character of our governments. … The injury which may possibly be done by defeating a few good laws will be amply compensated by preventing a number of bad ones." FEDERALIST PAPERS No. 73, 444 (Hamilton).

[139] That, at any rate, is Madison's confident conclusion at the end of FEDERALIST PAPERS No. 51 (at 325): "In the extended republic of the United States, and among the great variety of interests, parties, and sects which it embraces, a coalition of the majority of the whole society could seldom take place on any other principles than those of justice and the general good."

supermajorities.[140] It is appropriate that they should have to do so, for the state laws on which the negative operates come with a heavy suspicion of menacing sister-states and, hence, the union. In this fashion, the Constitution makes the safeguards against faction work once more against factionalism's most dangerous tendencies at the state level.

James Madison—the Madison of the Convention—was, as noted, deeply skeptical of the attempt to divide the universe of state activity so neatly into largely harmless, internal measures and dangerous, external stuff. Its proponents, he thought, mistook the outward symptoms of factionalism for the disease itself, and the clever design of arresting factions at the state borders grossly underestimated their capacity for obstinacy and evasion. Madison may well have been right in that assessment; in fact, any plausible argument for the dormant Commerce Clause—a pristine but judge-made negative against state laws that discriminate against or exploit sister-states in interstate commerce—must rest on an acknowledgment that the Madison of the Convention *was* right.[141] That consideration, though, rather strengthens the case for enforcing the negatives that are in the Constitution.

---

[140] Arguably, this overstates the point. Whereas affirmative federal legislation is of course subject to presentment and presidential veto, the state activities listed in Art. I, Sec. 10 are subject only to the consent *of the Congress*, thus rendering approval of compacts somewhat easier to obtain than ordinary legislation. The language, though, has been interpreted, at least by the political branches, as requiring executive as well as congressional consent. President Franklin D. Roosevelt vetoed a congressional consent resolution to a state compact, whereupon the resolution was amended and re-submitted to the President in an acceptable form. FREDERICK ZIMMERMAN & MITCHELL WENDELL, THE INTERSTATE COMPACT SINCE 1925, 93-94 (1951). In other words, the Compact Clause has been understood to require not approval by Congress alone but approval by Congress, *acting in the way in which Congress ordinarily approves legislation—i.e.*, subject to presentment, veto, and possibly judicial review. On that interpretation, the constitutional negative fully reverses the burden of producing a supermajority.

[141] For an explicit argument to this effect, running precisely parallel to the argument just made in the text, *see* DANIEL SHAVIRO, FEDERALISM IN TAXATION 70-71 (1993).

C. Risk-Free Federalism?

In subjecting state compacts to the ordinary operation of the Supremacy Clause rather than the negative, the Supreme Court has never denied the *existence* of the institutional risks that induced the Founders to subject any and all state agreements to a congressional negative. Rather, the functionalists on and off the bench have minimized those risks by painting the congressional negative as grossly overinclusive even in the areas to which the Founders limited it.

The *locus classicus* is Justice Field's dictum in *Virginia v. Tennessee*. By way of illustrating that a literal interpretation of the Compact Clause would sweep far too broadly, Field adduced four examples—one state's purchase of a "small parcel of land," within its own boundaries, that is owned by another state; a state's shipment of goods belonging to it through another state, on mutually agreeable terms; an agreement among neighboring states to drain a "malarious and disease-producing district" that crosses the border separating the states; and state cooperation for the purpose of preventing a "threatened invasion of cholera, plague, or other causes of sickness and death."[142] In such cases, Justice Field proclaimed, congressional consent can "hardly be deemed essential"; indeed, to require it under a literal reading of the Compact Clause would be "the height of absurdity."[143]

Field's examples fall remarkably short of making their intended point. In the first two examples, the states act as market participants and as parties to a private-law contract, not as sovereign political entities. Such activities should not fall under the

---

142 *Virginia v. Tennessee*, 148 U.S. at 518.

143 *Id.*

Compact Clause under any construction.[144] The fourth example—the aversion of an imminent health threat—can plausibly construed as falling under an implied necessity exemption to the Compacts Clause, in analogy to the clause of Art. I Sec. 10, immediately following the Compact Clause, that permits the states to wage war, without congressional consent, when they are under attack.[145] As for the drainage of a border-crossing swamp, one need not be an unreserved supporter of federal wetlands regulation to recognize that the activity might very well be of interest to the Congress. The swamp, for instance, might well surround a navigable stream, in which case it would be of interest to and under the jurisdiction of the federal government, and, moreover, of interest to downstream states.[146]

Field's difficulty in identifying more compelling examples to illustrate the excessive sweep of the Compact Clause is a sign of the times, or perhaps the Justice's limited imagination. *Virginia v. Tennessee* was issued before the uniform state law movement; before the Progressive endeavor to marry local control with national

---

144 Engdahl, *Interstate Arrangements*, 64 MICH. L. REV. at 88 n. 131.

145 Madison, in advocating an across-the-board negative, was willing to grant an exception in cases of urgency. *E.g*., 1 RECORDS OF THE FEDERAL CONVENTION 168 (Madison's notes). Arguably, the explicit constitutional provision for a "necessity defense" in case of war is an argument against inferring or implying it in the Compact Clause. I do not find that objection fully persuasive: the need for such an exception is simply more obvious in the case of physical attack. In any event, Fields' example has force only if the Compact Clause is read to require *prior* congressional consent. At the time of *Virginia v. Tennessee*, however, it was well established that congressional consent may be given after the fact, *see, e.g., Biddle v. Green*, 21U.S. (8 Wheat.) 1 (1823). That holding was explicitly reaffirmed in *Virginia v. Tennessee*, 148 U.S. at 521 ("[W]here the agreement relates to a matter which could not well be considered until its nature is fully developed, it is not perceived why the consent may not be subsequently given.").

146 *Cf. Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159 (2001) (federal jurisdiction under the Clean Water Act, 33 U.S.C. 1251*et seq.,* extends to all waters connected to navigable waters but not to isolated ponds or wetlands). Justice Field clearly intended to supply an example of a state agreement that no sensible person could possibly oppose. The fact that we now see valuable wetlands where Field and his contemporaries saw murderous swamps should caution against exempting state arrangements from the Compact Clause on the grounds of their "obviously" beneficial effects.

ambitions; before the emergent efforts to find "regional solutions for regional problems," such as metropolitan areas that transcend state boundaries; before the distribution of federal income tax proceeds under grants-in-aid programs to the states—in short, before the cooperative enthusiasms that would in due course mow down federalism's forms and formalities. Field's re-interpretation of the Compact Clause in *Virginia v. Tennessee* is at bottom committed to a dual federalism: it seeks to separate the federal government from the states, by discouraging a Compact Clause interpretation that might prompt needless entanglement. The examples that purport to make the case for a limited, functional analysis of the Compacts Clause are thoroughly traditional ones—police power stuff that states had done since the founding and, indeed, before the founding. Precisely not the sorts of activities that states might want to undertake in a modern society beyond the Founders' ken and contemplation. For all its flaws, *Virginia v. Tennessee* seeks to capture the Founders' intention, not to re-interpret the Compact Clause for the perceived needs of a modern society.

Later generations conveniently overlooked the context of *Virginia v. Tennessee* and instead instrumentalized its dictum for cooperative ends. The idea that Justice Field, that diehard common lawyer and dual federalist, should be mobilized for the Progressive enterprise is ironic and perhaps absurd, but not altogether unintelligible: if the Compact Clause is overbroad even with respect to the sorts of state agreements the Founders did have in mind, why should the Clause apply to new, emerging state agreements, spawned and necessitated by an increasingly complex and interdependent industrial society, that the Founders could not possibly have contemplated?

To put the rhetorical question into its most tenable declarative form: the universe of patently unproblematic state agreement has expanded to the point of justifying a departure from the congressional negative and a return to ordinary supremacy. If the Compact Clause negative operates—contrary to the Founders' fears—on a universe of transactions that, on balance, do more good than harm, then the objections that were successfully voiced at the Convention against the general negative may also apply to retaining the negative for state compacts—undue and unnecessary interference with affairs that concern only the states; useless demands on an already over-extended Congress; a needless nationalization of regional problems.

On that theory, the *U.S. Steel* Court may have been right, in a functional (though obviously not a textual) sense, to revert to the supremacy arrangement. If, on the other hand, state agreements do pose special risks, the calculus becomes more complicated: the functional inquiry turns into a search for a Compact Clause rule that would excise those special risks without, at the same time, wiping out the gains that might be had from state cooperation.

IV. The Risks of Cooperation

The most plausible case for lifting the congressional negative, I suggested at the outset, rests on a transaction cost model. States, no less than individuals, can strike Coasean bargains and realize gains from trade, provided the transaction costs are sufficiently low.[147] The Compact Clause negative, the argument goes, drives up

[147] The theoretical origin of "Coasean" bargains that re-arrange entitlements relative to the legal background norms is of course Ronald H. Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1, 2-8 (1960).

transaction costs; it should therefore be jettisoned. Instead of erecting obstacles, the central authority should define the states' property rights, enforce their bargains, minimize the transaction costs, and otherwise stay out of the way.

Upon inspection, this functional case for a latitudinarian Compact Clause proves untenable. The transaction cost model embodies non-trivial assumptions about property rights, externalities, competition, and agency. In transactions among (state) governments, those assumptions cannot be taken for granted, and are in fact quite unlikely to obtain. We therefore have no reason to assume that interstate agreements will automatically enhance efficiency. That observation alone casts doubt on a sanguine functional view of the Compact Clause.

One can go further, though: a sensible transaction cost perspective in fact suggests that state agreements pose special risks—that is, risks over and above those that attend to the individual, uncoordinated exercise of state sovereignty in a federal republic. Those risks are interrelated and partially congruent; for purposes of exposition and analysis, I classify them as follows: (1) state bargaining with federal rights and prerogatives; (2) the imposition of externalities on third-party states; (3) cartelization, meaning state agreements in restraint of economic and political competition; and (4) agency problems, meaning a diffusion of political accountability (often, though not always, through the creation of multistate authorities.) Jointly and severally, these distinct risks warrant something more in the way of federal safeguards than mere supremacy—something like

---

The general assumption is that minimal transaction costs will routinely generate Coasean bargains. For a critical discussion of this assumption see Robert D. Cooter, *The Cost of Coase*, 11 J. LEGAL STUD. 1, 15-20 (1982). For an explicit (and appropriately circumspect) application to interstate compacts *see* Thomas W. Merrill, *Golden Rules for Transboundary Pollution*, 46 DUKE L. J. 931 (1997). For a sophisticated analysis of horizontal jurisdictional cooperation, coupling a Coasean analysis with a game-theoretical approach, *see* ROBERT D. COOTER, THE STRATEGIC CONSTITUTION 108-115 (2000).

the Compact Clause. Though couched in the language of modern transaction cost and public choice theory, the analysis vindicates the Founders' special fear of state agreements and their understanding of a written, federal Constitution.

A. Compact Risks

Uncertain Rights. Coasean bargains presume that actors bargain with what they own. Put differently, efficient bargaining presupposes clearly defined property rights. "States' rights," however, are not so defined, and cannot be so defined. Federalism means that the national government and the states exercise sovereign authority over the same citizens and territory, which in turn means that their respective rights overlap. State compacts and agreements therefore pose a risk that states will bargain with assets that belong not to them but rather, or also, to the federal government.

Boundary settlements—for much of American history, the most common form of state compacts—provide an example. A bilateral bargain through which the Commonwealth of Virginia acquired half of West Virginia's territory may be the best for all concerned (at least in the party states), but it would also affect the allocation of seats in the House of Representatives. (For all we know, the seats may have been a bargaining chip in the transaction, if not its point.)[148] The bargain need not run afoul of the *U.S. Steel* test: it does not enhance the power of "the states," collectively, quoad the national government, and it does not adversely affect the political power (in the House of

[148] The point of the admittedly unrealistic hypothetical is simply to illustrate the unworkability of the *U.S. Steel* test. As a matter of curious historical fact, the possibility of a state-sponsored leveraged buy-out of a sister state was raised in an 19th-century boundary case arising under the Compact Clause: "By the compact of 1820, Tennessee acquired nearly half a million of acres …; if she could go ten miles north, she might two hundred, and purchase out a sister state, sapping the foundations of the Union." *Poole v. Fleeger*, 36 U.S. (11 Pet.) 185, 206 (1837) (John Catron, counsel for defendant in error) (quoted in Engdahl, *Interstate Arrangements*, 64 MICH. L. REV. at 81 n. 820).

Representatives) of any state except West Virginia—which explicitly agreed to the deal. That, however, proves only that the test is wrong. West Virginia's seats in the House are hers, but not in the same sense in which Ron Coase's farmer owns his cattle. They are part of a larger institutional arrangement and agreement, and may therefore not be alienated or acquired without congressional consent. The same is true of all powers in the federal domain, including those that are concurrently exercised by the states.

To be sure, states may also encroach upon the federal domain when acting individually—for instance, by erecting obstacles to interstate commerce under the guise of police power regulation. The danger of incursion, however, is particularly pronounced when those powers are exercised by agreement. States are naturally disinclined to surrender their own sovereignty—that is, rights that are indisputably and exclusively theirs—to another state or to a compact agency. They are much more likely to bargain with rights which they exercise at the national government's sufferance. The MTC, for a splendid example, does not attempt to harmonize the tax treatment of wholly domestic transactions, or for that matter the tax credits and abatements through which states attempt to attract business—even though a reciprocal agreement on such matters might well improve locational efficiency, reduce transaction costs, and improve the fate of state governments.[149] Instead, the Compact governs only the taxation of interstate transactions—the concurrent domain of the federal government.

---

[149] Unlike protectionist measures that discriminate against outside parties, state favoritism (such as subsidies and selective tax exemptions) is generally not thought to violate the dormant Commerce Clause, on the theory that the costs of such measures fall entirely, or very nearly so, on the state's own citizens. Few economists, however, consider this industrial-policy race to the bottom efficient, and state officials have long complained about the effects on their treasuries. *See, e.g.*, Melvin Burstein & Arthur J. Rolnick, *Congress Should End the Economic War Among the States*, 10 STATE TAX NOTES 1895 (1996). Even so, the MTC has confined its mandate to *interstate* taxation.

Concurrently held rights are not only worth less than full sovereignty rights (since they may be abrogated at any time); their exchange also holds a prospect of defeating the national government's claims through a kind of joint political preemption in reverse. State regulatory compacts very often come about under the threat of impending federal legislation—in other words, when (and because) a sluggish Congress is approaching the point of exercising federal supremacy. The creation of the Multistate Tax Compact, for a prominent example, "was more a reaction to the 'evils' of possible federal intervention than a pure reaction to the problems of diversity."[150] Almost by definition, such "defensive" state compacts regulate issues that, in the language of the *U.S. Steel* Court, are of "interest" to the national government in a theoretical and in an immediate, practical sense—and precisely not matters that arguably lie in the states' own exclusive domain.

There is no reason to expect that (state) bargaining with non-exclusive rights, without the consent of the co-owners, is efficient. Precisely when "states' rights" are non-exclusive, however, they are most likely to become a subject of state bargaining. For that reason, state agreements are, as a class, more suspect than ordinary, unilateral exercises of state powers. Unclear property rights assignments imply that the co-owners of those rights must be consulted on their exchange. The Compact Clause, as written, ensures that consultation. Its modern interpretation does not.

Externalities. Consistent with a regime of clearly assigned property rights, the Coasean model assumes that the parties will bargain over externalities and assign

[150] Jerry Sharpe, *State Taxation of Interstate Businesses and the Multistate Tax Compact: The Search for a Delicate Uniformity*, 11 COLUM. J. LAW & SOC. PROBS. 231, 244 (1975) (hereafter Sharpe*, State Taxation*).

responsibility and costs one way or the other—as distinct from fobbing them off on a third party. A federal system of three or more states, however, enables two (or more) states to inflict externalities that neither of them, acting on its own, may be able to induce. Consider Justice Field's example of draining a malarious bi-state swamp: while the benefits of that bargain would (by definition) not be attainable by compacting States A and B, acting individually, neither would the externality—water loss—to downstream State C.[151]

Cartelization. State agreements that restrain policy and economic competition to the detriment of another state are a species of externalities—one that preoccupied the Founders. New Jersey, lacking a viable port, was at the mercy of New York and Philadelphia, both of which taxed goods destined for New Jersey. Alluding to a then-current metaphor, Madison compared the state to "a cask bottled up at each end" and North Carolina, likewise lacking a deep-sea port, to a "patient bleeding at both arms."[152] By virtue of their resources, location, or history, some states will always be in a more advantageous position than others; that cannot be helped. What *can* be helped is the anti-competitive and, in particular, the collusive exploitation of that advantage.[153]

---

151 The analysis holds under any assumption about political dynamics at the state level. States A and B may want to push the externalities downstream for any number of reasons—local producer demand; an authentic reflection of domestic voter demand for public goods; or the sheer impossibility of ascertaining third-party externalities. *See* David N. Copas, Jr.*, The Southeastern Water Compact, Panacea or Pandora's Box? A Law and Economics Analysis of the Viability of Interstate Water Compacts,* 21 WM. & MARY ENVTL. L. & POL'Y REV. 697, 722-23 (1997).

152 James Madison*, Preface to the Debates in the Convention,* in NOTES OF DEBATES IN THE FEDERAL CONVENTION OF 1787, at 7 (Koch ed., 1984).

153 Saul Levmore, *Interstate Exploitation and Judicial Intervention*, 69 VA. L. REV. 563 (1983) (hereafter Levmore, *Interstate Exploitation*), argues that the prevention of interstate exploitation (as distinct from non-exploitative state interferences with interstate commerce) should serve and, by and large, has served as the foundation of the Supreme Court's jurisprudence under the dormant Commerce Clause and

New Jersey's particular predicament was remedied through the Import-Export Clause,[154] rendering the Compact Clause redundant in this case. (If New York and Pennsylvania may not individually levy duties on goods destined for or coming from New Jersey, they may not do so by agreement, either.) State cartels to the detriment of third states need not, however, involve practices that are forbidden by an independent constitutional provision. When a particular commodity—say, oil—is available in ten states but vital to all fifty, the producer states' advantage may cause a problem of a constitutional magnitude even when competition among the supplier states prevents the exploitation of consumer states.[155] If the suppliers form an oil compact to restrict output and raise prices, the problem is clear and manifest.

Such a domestic OPEC did in fact exist, complete with its own Saudi Arabia (Texas, which at the time of the formation of the Interstate Compact to Conserve Oil and Gas in 1935 controlled about half of all then-known U.S. oil reserves). That state compact, like other natural resource compacts,[156] was formed with congressional

---

related constitutional provisions. As Levmore notes, *id.* at 570 n. 17, the Compact Clause "can be interpreted to reflect the theme of [his] article." When states collude, exploitation of sister-states is so likely "that Congress is called in to review the arrangement at the outset." *Id.* The exposition, here and below, of interstate exploitation as a Compact Clause risk is consistent with Levmore's suggestion and Commerce Clause analysis.

154 U.S. Const. Art. I Sec. 10 Cl. 2 ("No State shall, without the consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing it's inspection laws.") *See* the discussion in *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 283-84 (1976).

155 The clearest example is the imposition of severance taxes for raw materials. *See, e.g.*, *Commonwealth Edison v. Montana* , 453 U.S. 609 (1981) (sustaining coal severance tax against constitutional challenge). The constitutionality of such taxes under the dormant Commerce Clause is a genuinely difficult question. For excellent discussions *see* Levmore, *Interstate Exploitation*, 69 VA. L. REV. at); and Stephen F. Williams*, Severance Taxes: The Supreme Court's Role in Preserving a National Common Market for Energy Supplies*, 53 COLO. L. REV. 281 (1982)..

156 For example, three marine fisheries compacts were formed during the 1940s. For an account of the first and largest of these compacts, establishing the Atlantic States Marine Fisheries Commission, *see* BARTON, INTERSTATE COMPACTS 22-33.

approval,[157] and its history nicely illustrates the purposes and effects of the Compact Clause negative. Under the *U.S. Steel* rule, the oil-producing states could have established and managed their cartel unless and until Congress affirmatively exercised its powers under the Commerce Clause and the Supremacy Clause. The benefits of the arrangement, though, were more concentrated—on the producer cartel's member-states—than the costs to the consumer states. Affirmative legislation would have forced anti-cartel states to overcome that hurdle, as well as the federal supermajority requirements. The Compact Clause negative, in contrast, forced the supplier states to attract votes from consumer states (through logrolling, or by diluting the cartelizing effects). That dynamic prompted earnest and vigorous assurances, on the part of the producer states, that their arrangement was not a price-fixing cartel (which is of course precisely what it was, though not a terribly successful one).[158] Nonetheless, a requirement for periodic congressional reapproval contained in the Compact generated increasingly stringent federal oversight and control over the Compact and its administration.[159]

The threat of cartelization extends not only to the exploitation of natural resource advantages and bottlenecks (such as deep-sea ports) but also to policy arrangements. Suppose that fifteen labor-dominated states in a nation of twenty states wish to maintain "living wage" requirements within their own jurisdictions. Suppose further that they agree, by compact, to "harmonize" their living wage requirements and moreover, to

---

157 Interstate Compact to Conserve Oil and Gas, 49 Stat. 939 (1935).

158 BARTON, INTERSTATE COMPACTS at 12-17. The cartel's effectiveness was hampered by the emergence of new oil-producing states, which undermined the chief producer state's (Texas) ability to maintain supply and price discipline. *Id.* at 16-17.

159 *Id.* at 14-15. While the Compact still exists, the radically different market conditions of the early 1970s rendered its output ceilings superfluous. ROBERT L. BRADLY, JR., OIL, GAS, AND GOVERNMENT: THE U.S. EXPERIENCE 104-06 (1996).

purchase goods exclusively from manufacturers that (a) pay the agreed-upon wage and (b) refuse to do business with suppliers that do not. Under suitable conditions, the cartelists may—given, for example, substantial market power and high exit costs—succeed in wiping out the competitive advantages that the five dissenting states have chosen to preserve. Or suppose several states—those that aren't domiciles for large, integrated insurance companies—agree to deny a business license to any insurance company that refuses to write policies, for any business line (such as car insurance), in any state of the union.[160] The exercise of federal supremacy to trump such cartels would have to overcome supermajoritarian obstacles. The Compact Clause reverses that burden and, in doing so, provides a measure of security against collusive interstate exploitation.

Agency and Delegation Problems. Pure transaction cost models presuppose a symmetry of incentives, if not actual identity, between principals and agents. Transactions among governments, however, may involve significant agency problems. Such problems are particularly likely to arise under intergovernmental cartel arrangements. In fact, every such cartel will also present agency and delegation issues.

Agency problems are probably negligible when state bargains are one-shot deals. An agreement by two states to demarcate more precisely an agreed-upon boundary—the subject of *Virginia v. Tennessee*—is an example: The benefits—such as the avoidance of needless disputes in the future—are roughly symmetrical. Barring unusual circumstances, neither side has reason to expect that the other side will benefit disproportionately.

---

[160] Several individual states have imposed equivalent exit restrictions on insurance companies. *See* Richard A. Epstein, *Exit Rights Under Federalism,* 55 LAW & CONTEMP. PROBS. 148, 161-165 (1992).

Legislative approval in the compact states confirms a final assignment of mutual rights and obligations. The deal can be implemented without extensive cooperation and monitoring by the parties. Under those circumstances, there is no reason to suspect an asymmetry of incentives between the governors and the governed.

Regulatory state bargains, in contrast, often involve the allocation of funds and, consequently, disputes over the parties' relative (financial and institutional) contributions.[161] Such compacts typically attempt to regulate complex arrangements that are subject to change, either because natural circumstances change (as is often the case in compacts dealing with water rights) or because private actors adjust their conduct in response to new (compact) law. Moreover, questions may arise as to how the gains from cooperation are to be distributed. *Ex ante*, the distributive question invites strategic gamesmanship.[162] *Ex post*, it compels the parties to monitor each other's performance and to establish formulas and mechanisms for the periodic allocation of contributions and gains. The costs of doing so rise in proportion to the number of players and the complexity and duration of the cooperative venture.

The monitoring costs are high even for the agents, meaning state legislatures. For the citizen-principals, the costs are prohibitive. By way of a simple example, let five states (A-E) are the exclusive producers of consumer good "X." Powerful producers in each state would very much like their government to increase the price of X, but cannot do so because consumers would purchase more X from one of the four rival states. Suppose, however, that the governors of A-E agree to impose a surcharge on X-sales, to

---

161 Robert G. Dixon, Jr., *Constitutional Bases for Regionalism: Centralization; Interstate Compacts; Federal Regional Taxation*, 33 GEO. WASH. L REV. 47, 58 (1964).

162 ROBERT D. COOTER, THE STRATEGIC CONSTITUTION 60-62, 110-112.

be shared by the state government and the producers (in some proportion): all producers and all governments will be better off. All consumer-citizens will be worse off.[163]

Rent-seeking at the state level, of course, is an ordinary phenomenon, as is the temptation of beggar-thy-neighbor policies. State agreements, however, exacerbate those risks. First, state cartels will on some margin dampen jurisdictional competition and dilute the citizens' exit rights that would otherwise discipline rent-seeking. Second, a state (A) that intends to beggar its neighbor (B) does not really intend to beggar B, *as a state*; it intends to beggar B's citizens. State B, meanwhile, has the same purpose in mind vis-à-vis A. The agents of A and B, in other words, have symmetrical incentives to exploit each other's citizens.[164] Unless government agents are perfectly monitored, state agreements provide them with opportunities to procure, for governments, benefits that neither state could procure individually—while exposing citizens to risks that they would not incur if such agreements were subject to special impediments, or prohibited altogether.

Compacts seeking to establish an on-going cooperative regime—as distinct from agreements that conclusively settle mutual claims and rights—virtually always require a standing board or commission, since somebody must monitor the parties' performance, secure their cooperation, and allocate and distribute the gains. Such bodies exhibit delegation problems in a particularly acute form and, in practice, have consistently been found to elude democratic control and accountability. Beginning with the scandal-

---

[163] The tobacco cartel established by the MSA is a variation on this theme. *See infra* nn. and accompanying text.

[164] They also have symmetrical incentives to exploit *their own* citizens by disguising the true cost of government programs. The imposition of sales tax (more precisely, use tax) collection obligation on out-of-state sellers is an example of this stratagem.

plagued New York-New Jersey Port Authority—the first compact commission, and Frankfurter's and Landis's paradigmatic example of fruitful state cooperation[165]—compact commissions have proven to be poorly supervised even by state legislatures (not to mention voters), and thus prone to mismanagement and bureaucratic empire-building.[166] The notion that a state legislature can bind its successors by consenting to a state agreement that can be terminated only with the consent of other states—as is the case under compacts that do not provide for the option of a unilateral withdrawal—raises additional problems of democratic governance and accountability.[167]

---

[165] *See* Frankfurter & Landis, *The Compact Clause*, 34 YALE L. J. at 697-98. On the scandals and mismanagement at the Port Authority, which prompted a congressional investigation and an acrimonious political confrontation between the Authority and the Congress, *see* Emmanual Celler, *Congress, Compacts and Interstate Authorities*, 26 LAW & CONTEMP. PROBS 682 (1961).

[166] The most impressive empirical demonstration of the diffusion of accountability and loss of public control that characterizes compact commissions is MARIAN E. RIDGEWAY, INTERSTATE COMPACTS: A QUESTION OF FEDERALISM 308-09 (1971). *See also* Jill Elaine Hasday*, Interstate Compacts in a Democratic Society: The Problem of Permanency*, 49 FLA. L. REV. 1 (1997); and Note, *Charting No Man's Land: Applying Jurisdictional and Choice of Law Doctrines to Interstate Compacts*, 111 HARV. L. REV. 1991, 1995 and *id.* n. 29 (1998).

Compact commissions, existing off the constitutional charts somewhere between the national governments and the states, pose serious constitutional questions even when they are created or, as the case may be, approved by Congress. *See Virginia v. U.S. EPA*, 108 F.3d 1397 (D.C. Cir. 1997) (discussing constitutional questions presented by Ozone Transport Commission established under Clean Air Act, 42 U.S.C. 7511c; case decided on independent statutory grounds). In these instances, however, the commission's life can be terminated by the single, superior body that created it in the first instance. (States may, by virtue of the same logic, create inferior counties and districts and delegate their police powers to those entities.) In contrast, states cannot unilaterally terminate the life of an interstate agency they have helped to create. Thus, such agencies pose a special and particularly urgent delegation problem. Robert G. Dixon, Jr., *Constitutional Bases for Regionalism: Centralization; Interstate Compacts; Federal Regional Taxation*, 33 GEO. WASH. L REV. 47, 73-75 (1964).

[167] Hasday, *supra* n. at 2-3. Some scholars have argued that cooperative state arrangements requiring continuous cooperation and standing compact commissions are beyond the purview of the Compact Clause. The Founders, those commentators claim, intended the Clause to apply to agreements that conclusively determine the rights between the parties; agreements that fail to do so should *ipso facto* be exempt from the Clause. *See, e.g.*, Engdahl, *Interstate Arrangements*, 64 MICH. L. REV. at 97-101; Robert M. White, *The Constitutionality of the Multistate Tax Compact*, 29 VAND. L. REV. 453, 458-59, 462 (1976). The Multistate Tax Commission advanced this argument in the *U.S. Steel* litigation. Appellee's Brief at 36, *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452 (No. 76-635). That, however, was the one argument that the Supreme Court opinion (in virtually all other respects, a toned-down recitation of the MTC's brief) did not endorse—perhaps, because the Court had already held state compacts of whatever description to be effectively immune from the congressional consent requirement; perhaps, because the claim was too much

B. Constitutionalism

The risks just identified are hardly unique to state compacts. Congressional legislation—not just compact approval, but legislation *per se*—poses very similar risks. Federal statutes routinely favor some states over others, substitute policy cartels for state competition, and exploit through (vertical) schemes of intergovernmental cooperation the "slack" that is produced by the imperfect monitoring of state and federal politicians.[168] Nor has Congress proven immune against the temptation of establishing interstate agencies off the constitutional charts, from the Tennessee Valley Authority to the Ozone Transport Commission.[169] Obviously, Congress cannot trample on federal prerogatives, but that advantage is compensated, in a manner of speaking, by comparable disadvantages attendant to federal legislation—for instance, the undesirability of a uniform national solution for problems that may be regional in scope. In that light, we may wish to tolerate high-risk state bargains, rather than cramming compacts, or issues that could be addressed through compacts, into the United States Congress.

The objection has a certain surface plausibility, but it misses constitutionalism's point. Under any federal system, states will show tendencies toward parochialism and mutual exploitation—the centrifugal tendencies that so distressed and alarmed the

---

even for a Court that was otherwise unperturbed by constitutional considerations. Off-the-charts compact commissions are obviously more problematic than run-of-the-mill boundary settlements. The fact that such fourth-branch-of-government constructs would have blown the Founders' minds cannot justify their exclusion from the Compact Clause.

168 The potential for bilateral exploitation of agency problems and collusion between state and federal officials is the central argument against the federal "commandeering" of state officials. *See New York v. United States*, 505 U.S. 144, 183 (1992); *Printz v. United States*, 521 U.S. 898, 929-30 (1997). For the application of this argument to the Compact Clause *see infra* nn. and accompanying text.

169 *See* Tennesse Valley Authority Act, 16 U.S.C. 831 *et seq*.; Clean Air Act, 42 U.S.C. 7511c (Ozone Transport Commission). *See also* Gramm-Leach-Bliley Financial Modernization Act, P.L. 106-102, 113 Stat. 1338 (creating incentives for formation of state insurance regulatory compacts).

Founders. No Constitution can suppress the states' political games without entirely abolishing states as quasi-autonomous entities. What a Constitution can and must do, however, is to coordinate the games, such that the equilibria remain within a range that is generally perceived as tolerably fair and efficient.[170] To that end, a Constitution allocates powers and specifies the composition and procedures of the coordinating institutions.

Our own Constitution ameliorates the specific risks of state compacts in two related ways. First, the congressional approval requirement guarantees that every state will be informed of, and be heard on, sister states' agreements. In this manner, the Compact Clause reduces the costs each state would otherwise incur in monitoring and countermanding cartels, collusion, and combinations adverse to its own interests. Second, supermajority requirements provide a measure of protection against parochial state combinations to the detriment of the non-consenting states.

One can plausibly argue that these are the rules that states would choose behind a pre-constitutional veil of ignorance. The protections are not cost-free: they defeat some future bargains that some states might find in their interest. Even state bargains that some states find useful, and none find objectionable, might be held up or hijacked by the Congress. That price, however, may be worth paying for effective protection against the horrendous risk of becoming a victim of collusion among (supposedly) sister states. In any event, the Compact Clause negative is the coordination mechanism that the Founders did in fact choose, and if constitutionalism means anything, it means that the players may not defect to some other coordination mechanism when that happens to be in their short-term interest. A federal Constitution must ensure that bargains among states are made in

---

[170] On the notion of a Constitution as a means of coordination *see* Peter C. Ordeshook, *Constitutional Stability*, 3 CONST. POL. ECON. 137 (1992).

the agreed-upon place and manner, *and nowhere else*. A Constitution that fails to hold the players to their pre-commitment strategy is a mere treaty of convenience.[171]

V. Multistate Taxation: A Second Look

This Part applies the preceding analysis of compact risks to the Multistate Tax Compact of *U.S. Steel* fame; the following Part VI performs the same operation on the

---

[171] *Id.* at . ("treaty of convenience"). No federal system permits unsupervised, separate side-agreements among member-states. See, e.g., German Constitution Art. 32(3) (authorizing states to conclude treaties on matters within their legislative competence and "with the consent of the federal government" [Bundesregierung]. Although the Article speaks of treaties with foreign countries, it is commonly understood to authorize treaties among the *Laender*). Even looser, non-constitutional confederations typically preclude such defections. A highly instructive contemporary example is the European Union. EC Treaty Art. 11 (ex 5a) provides as follows:

> 1. Member States which intend to establish closer cooperation between themselves may be authorized [by the European Council] to make use of the institutions, procedures and mechanisms laid down by this Treaty, provided that the cooperation proposed:
>   (a) does not concern areas which fall within the exclusive competence of the Community;
>   (b) does not affect Community policies, actions or programmes;
>   (c) does not concern the citizenship of the Union or discriminate between nationals of Member States;
>   (d) remains within the limits of the powers conferred upon the Community by this Treaty; and
>   (e) does not constitute a discrimination or restriction of trade between Member States and does not distort the conditions of competition between the latter.

See also TEU Art.43, 44 (ex K.15, K.16). Art. 11 is a kind of Compact Clause-plus. *All* member-state cooperation within the scope of the European Treaties is subject to approval by the Council, and even the Council may approve cooperative ventures only under very limited conditions. (*See, e.g.*, Jo Shaw, *The Treaty of Amsterdam: Challenges of Flexibility and Legitimacy*, 4 ELJ 63 (1998). The universe of unapprovable cooperative ventures is the equivalent of the U.S. Constitution's absolute prohibition on state treaties. The list of features that render proposed cooperation unapprovable, and especially the injunction against cartel arrangements in restraint of interstate trade, runs parallel to the compact risks explicated in this Part.

Art. 11—most of which was added to the EC Treaty in the Treaty of Amsterdam (1999)—attempts to facilitate closer cooperation among EU members so inclined, without having the pace of integration dictated by the slowest member. (For a brief discussion *see* STEPHEN WEATHERILL & PAUL BEAUMONT, EU LAW (3rd ed. 1999) 23-27 and sources cited *id.* nn. 74-79). That endeavor, though, runs up against the baseline premises and purposes of the European Treaties—non-discrimination, equality among member-states, and the supermajority requirements and other procedural protections that the established European institutions afford dissident member-states. The narrow scope of EC Treaty Art. 11 reflects a jealous effort to safeguard those protections. In precisely the same fashion, the Compact Clause precludes states from creating a Constitution at variance with the one we actually have.

1998 Master Settlement Agreement between tobacco manufacturers and state attorneys general. Both agreements are cartels; both pose massive agency and delegation problems; both infringe on the constitutionally protected interests of the union and of sister states. Both agreements, and all similar state agreements present and future, are unconstitutional under any reasonable Compact Clause analysis.

A. The MTC as a Tax Cartel

Like any decentralized tax system, the state taxation of interstate business income abounds with coordination problems.[172] The Supreme Court's decision in *Northwestern States Portland Cement*,[173] permitting the "fair apportionment" of interstate business income in every state where the taxed entity has a "nexus," entailed that a single sale might be taxed in four different states, each time under a different allocation and apportionment formula.[174] Thus, business income could easily be taxed on more than 100 percent of its base. Paradoxically (and worse, from the states' perspective), taxable income could escape taxation altogether.

The MTC's stated mission, as noted, is to address these problems through political harmonization. From the outset, though, the Compact was widely viewed as an attempt to establish a tax cartel. By the time of the *U.S. Steel* litigation, the MTC Commission had acquired an "image as the agent of a group of small states trying to

---

[172] Long before the Multistate Tax Compact, Frankfurter and Landis discussed state tax administration as a fruitful area for state cooperation. Frankfurter & Landis, *The Compact Clause* , 34 YALE L. J.at 704.

[173] *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959) (briefly discussed *supra* nn. and accompanying text).

[174] Sharpe, *State Taxation*, 11 COLUM. J. LAW & SOC. PROBS. at 238.

increase their revenues by 'feeding off' 'eastern' businesses,"[175] meaning businesses commercially domiciled in the eastern states. A simple thought experiment suggests that these impressions accurately reflect the MTC's nature and raison d'etre.

Tax coordination problems can in principle be solved without a political supra-state regulatory institution: states could agree, on a reciprocal basis, to tax all business income only in the company's domicile state, meaning the company's principal place of business or its state of incorporation.[176] Such a rule of origin or "mutual recognition" (as it is called by the European Union, which applies the principle to certain regulatory matters)[177] largely obviates the need for continuous political harmonization. While secondary questions (such as the definition of corporate subsidiaries) may require coordination, the origin rule is essentially self-enforcing: a company that receives a tax claim from a non-domicile state would obtain an injunction, and that would be the end of the matter. Mutual recognition, however, implies uninhibited tax competition. States would compete for business by lowering taxes and, all else equal, taxes would drop everywhere. If the domicile rule is the state of incorporation, the equilibrium tax rate is zero.

Naturally, states do not desire that outcome. In fact, it was precisely the traditional allocation of various forms of business income to domicile or origin states that prompted

---

175 Sharpe, *State Taxation* at 274 (footnote omitted).

176 I assume for purposes of illustration that all taxed businesses are U.S. corporations and that all their income is earned in the U.S. Multinational corporations and operations complicate but do not materially change the analysis.

177 The literature on mutual recognition within the European Union has reached torrential proportions, especially in European journals. A readily accessible overview is Wolfgang Kerber, *Interjurisdictional Competition Within the European Union*, 23 FORDHAM INT'L L. J. 217 (2000).

the MTC creation by mostly small states west of the Mississippi. (Those "market states," whose leading role earned the Compact its reputation as a tax cartel, have remained the backbone of the MTC's membership. Eastern corporate domicile states—New York, Massachusetts, Pennsylvania, Delaware, Virginia—never became full MTC members.)[178] Market states benefit from tax apportionment (rather than allocation), which subjects corporate income to taxation in any destination jurisdiction where a company does business, regardless of the company's domicile and structure. Complete apportionment of business income will completely eviscerate tax competition. Theoretically, uniform apportionment will also capture, for taxation purposes, no less (and no more) than 100 percent of total business income. A corollary of full apportionment rule is a principle of unitary taxation, which treats a corporation's subsidiaries as a single entity for purposes of taxation. This device prevents corporations from escaping taxation through clever corporate restructuring. Put less charitably, unitary taxation enables a state to capture a foreign corporation's income even if the corporation's subsidiary in the state earned no income or even incurred losses.

The Multistate Tax Commission has favored apportionment and unitary taxation *ab ovo*.[179] It has pushed these principles to the outer limits permitted by federal law and

---

[178] Over time, the MTC developed "associate" and "sovereignty" memberships, which do not require enactment of—or compliance with—the Compact. For the MTC's description *see* http://www.mtc.gov/ABOUTMTC/Mbershpdef.htm. Some non-Compact states have availed themselves of these opportunities. *See* http://www.mtc.gov/ABOUTMTC/Aboutmtc.htm (listing current membership)(visited Feb. 28, 2002).

[179] Article IV of the Multistate Tax Compact in substance constitutes the Uniform Division of Income for Tax Purposes Act (UDITPA) and, with it, a destination test for the calculation and apportionment of retail sale business income. Grossly oversimplifying a complicated reality, if a New York company that earns twenty percent of its income from sales in California, its income will for tax purposes be apportioned on that basis—even if the company has only a nominal presence in California.

constitutional constraints, and occasionally beyond those limits.[180] The MTC's purpose, in other words, is not tax harmonization *simpliciter*. Rather, its purpose is to achieve tax harmonization, *while suppressing (locational) tax competition*. One can quarrel over the extent to which the MTC has achieved that objective, and one can plausibly argue that the compact *cannot* fully succeed.[181] But the MTC's nature as a tax cartel is beyond peradventure.

B. Externalities

Obviously, the MTC Commission cannot impose its rules on non-member states. It can, however, dissipate some of the non-member states' competitive advantages. The *U.S. Steel* Court understood this point; Justice White's dissent made it explicitly.[182] Non-business dividend income, for instance, had traditionally been allocated to domicile states for purposes of taxation. Many of the big domicile states (such as New York) exempted such income from taxation. The MTC moved towards apportionment of dividend income among the states, thereby diluting tax competition on this margin and dissipating the non-taxing states' advantage.

Justice Powell's majority opinion readily conceded the point, but responded that the economic effects of the MTC's dividend regime on non-member states were no different from the "pressure" that states routinely experience as a result of regulatory or

---

180 *See, e.g.*, J. HELLERSTEIN & W. HELLERSTEIN, STATE TAXATION, VOL. I (CONSTITUTIONAL LIMITATIONS AND CORPORATE INCOME AND FRANCHISE TAXES) 9-85 (3rd ed. 1998) (MTC definition of business income "in the context of dividends appears overbroad both from a statutory and constitutional standpoint").

181 *See infra* nn. and accompanying text.

182 "Non-Compact States can be placed at a competitive disadvantage by the Multistate Tax Compact." *U.S. Steel Corp. v. MTC*, 434 U.S. at 495 (White, J. diss.).

tax decisions made by other states.[183] That is a lot like saying that a private firm need not fear price-fixing among its competitors because the competitors are permitted to take unilateral actions that might put the firm out of business. If the private market analogy fails to persuade, re-consider the analogy of physical interstate externalities: the unregulated use of a waterway may leave a downstream state dry, since upstream states will individually over-exploit the resource. It does not follow, however, that the upstream states may *agree* on an allocation that deprives the downstream state of water.[184] Interstate externalities are one thing. Externalities imposed by state agreement are a different beast.

C. Agency and Delegation

Under the MTC's joint audit and enforcement provisions, the Commission may subpoena any person beyond the borders of a member state requesting such a subpoena; under certain circumstances, it may also conduct joint audits *sua sponte*.[185] These powers—which, contrary to the *U.S. Steel* Court's representations,[186] "clearly exceed those of any member acting alone"[187]—create a situation in which political responsibility

---

183 *Id.* at 477-78.

184 The reason, briefly mentioned supra n. and accompanying text, is the shift from a (hypothetical) competitive baseline to collusion and exploitation. A compact-free environment permits the downstream state to obtain water from one of the upstream states at something close to a competitive price, whereas an upstream state compact creates a monopoly and exploitation.

185 MTC Art. VIII (3).

186 *See supra* n.

187 Robert M. White, *The Constitutionality of the Multistate Tax Compact*, 29 VAND. L. REV. 453, 465 (1976) (footnote omitted). The author defends the arrangement as inconsequential and akin to a reciprocity arrangement; *id.* at 465-66. *See also U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. at 492-93 (White, J., diss) (arguing that. the MTC possesses some coercive force over member states).

for a highly coercive exercise of sovereign authority gets lost in an intragovernmental shuffle.[188] The MTC plaintiffs provided compelling, unrebutted evidence of proceedings in which companies confronted a bewildering array of MTC and state auditors with uncertain and conflicting claims of authority.[189]

Similar problems characterize the Commission's regulatory authority. In the *U.S. Steel* litigation, the MTC described its regulations as inconsequential "recommendations." After all, the Commission argued, MTC regulations have no legal force unless they are adopted by the appropriate state officials through ordinary rulemaking procedures under state law. The Commission exercised no power the member-states could not also exercise individually, and in any event, each state remained free to withdraw from the Compact at any time.[190] The ready acceptance of those arguments by the *U.S. Steel* Court,[191] however, betrays at best a lack of realism and, at worst, willful blindness.[192]

---

188 Sharpe, *State Taxation* at 260 ((“Another tier of tax administration … makes it easier for responsibility for tax decisions to be ‘lost’ somewhere between the states and the MTC.”) A long footnote to the quoted sentence provides mind-boggling examples of abuses that the diffusion of responsibility invites.

189 Brief

190 MTC VII(3); Brief at

191 *See supra* n.

192 It also betrays a misunderstanding of the delegation point. No governmental body can “delegate” a power that it cannot exercise individually. A purported attempt to do so poses an *ultra vires* problem, not a delegation problem. Similarly, if the mere possibility of withdrawal sufficed to avert delegation problems, there could be no delegation of power by Congress, since Congress can always revoke a delegation of its powers. An irrevocable “delegation” is not a delegation but a constitutional amendment. A rule against delegation necessarily implies that governmental bodies may not transfer their constitutional powers to another body even for a limited duration.

Joining the Compact requires an act of state legislation; withdrawing from it requires a repeal of that statute.[193] This all-or-nothing quality lends genuine regulatory force to the Commission's rulings,[194] and the adoption of a particular MTC "recommendation" tells us next to nothing about the member-states' authentic preferences. The officials who are doing the adopting are typically not legislators but rather the tax commissioners who compose the MTC in the first instance. The legislature that consented to the MTC may never hear of the "recommendation" and its consequences. Thus, the effect of the Commission's "extremely influential" regulations[195] has been to enhance the fiscal policy-making authority of tax commissioners, who have adopted and enforced MTC "recommendations" at the outer limits and, at times, in contravention of applicable state law.[196] Even at the time of the MTC litigation, prominent tax experts complained that member-states viewed the MTC as a kind of "constitution" for a tax confederacy and its regulations, as akin to confederate statutes that preempt local law. They likewise worried about the attendant expansion of tax commissioners' fiscal authority.[197] Experience since has confirmed that their apprehensions.

---

193 MTC Art. X.2.

194 *See U.S. Steel v. MTC*, 434 U.S. 452, 493 (White, J. diss.).

195 J. HELLERSTEIN & W. HELLERSTEIN, STATE AND LOCAL TAXATION CASES AND MATERIALS 578 (6th ed. 1997).

196 *See, e.g.*, John C. Blase & John W. Westmoreland, *Quill Has Been Plucked! MTC States are Slowly Eroding the Substantial Nexus Standard*, 73 N. DAK. L. REV. 685, 708-710 (1997) (describing state adoption of MTC interpretive regulations, the so-called "Bulletin 95-1," in contravention of state statutory and case law); and Kaye Caldwell, *"Dispassionate" Debate on Bulletin 95-1?*, STATE TAX NOTES Aug. 27, 1996, at 20 (criticizing MTC's "total disregard for state law in asking the states to adopt" Bullentin 95-1).

197 Cite in U.S. Steel brief.

D. Federal Rights

Recall the *U.S. Steel* Court's refrain: the MTC might well affect the *interests* of the United States, but not the federal government's legal *supremacy*.[198] As explained, however, the Constitution subjects state compacts to a negative, rather than mere supremacy, because constitutional supermajority requirements will render the exercise of federal supremacy insufficiently protective of federal interests. That argument applies with particular force to interstate taxation.

Over the course of American history, Congress has intervened in the state taxation of interstate commerce only a handful of times and under very unusual circumstances.[199] Pleas for Congress to mend its ways, to mind its constitutional obligations, and to address a seemingly intractable subject-matter have been both common and futile. A congressional effort to find a general formula for the state taxation of interstate commerce *ipso facto* affects all states (in an existential fashion) and industries of every size and nature. Given the range and the intensity of the affected interests, the supermajoritarian difficulty becomes well-nigh insurmountable.[200] [201]

---

[198] *Supra* nn. and accompanying text.

[199] Apparently, the 1959 "moratorium" enacted in response to the Supreme Court's *Northwestern States Portland Cement*, *supra* nn. and accompanying text, represented the very first congressional intervention in the state and local taxation of interstate commerce. DANIEL SHAVIRO, FEDERALISM IN TAXATION 3-4 n. 10 (1993) (quoting and citing JEROME HELLERSTEIN & WALTER HELLERSTEIN, STATE AND LOCAL TAXATION 324. (5th ed. 1988) Congressional interventions have remained exceedingly rare. Walter Hellerstein, *State Taxation of Interstate Business: Perspectives on Two Centuries of Constitutional Adjudication,* 41 TAX LAWYER 37 (1987); and Kathryn L. Moore, *State and Local Taxation: When Will Congress Intervene*? 23 J. LEGIS. 171 (1997) (hereafter Moore, *State and Local Taxation*) (noting paucity of federal interventions between 1971 and 1996 and showing, *id.* at 173, "that the empirical evidence and public choice theory cast doubt on the likelihood of Congress ever enacting legislation mandating uniformity and state and local taxation.").

[200] With the exception of P.L. 86-272, the "provisional" but still-existing safe harbor that was hastily enacted after the Supreme Court's *Northwestern States Portland Cement* decision (*see supra* nn. and accompanying text), the few congressional interventions have typically come at the behest of individual, discrete industries or groups of taxpayers, such as railroads, pensioners, internet companies, and, naturally,

Judicial safeguards for federal supremacy are similarly inadequate. The state taxation of interstate commerce is subject to only minimal due process and equal protection constraints.[202] The Supreme Court's somewhat more stringent dormant Commerce Clause jurisprudence bars overtly unfair discriminatory state taxation, as well as state taxation that would unduly burden interstate commerce. In its most aggressive decisions, the Court has held that state taxes must (among other requirements) be "fairly apportioned," such that a state's apportionment formula, if applied by all states, would not result in double taxation.[203] However, the Court has refrained from imposing any particular apportionment formula, and it has permitted each state to adopt a "consistent"

---

members of Congress. *See* Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, sec. 306, 90 Stat. 31, 54-55 (current amended version codified at 49 U.S.C. sec. 11501); Act of Jan. 10, 1996, Pub. L. No. 104-95, 109 Stat. 979 (1996) (barring states from taxing pension income of nonresidents); Internet Tax Moratorium, stat cite ; Act of July 19, 1977, Pub. L. No. 95-67, 91 Stat. 271 (codified at 4 U.S.C. sec. 113 (1994)) (prohibiting state or local governments, other than jurisdictions from which member of Congress is elected, from treating legislator as resident for income tax purposes). *See generally* Moore, *State and Local Taxation*, at 172-73 *et pass*. (evidence on congressional intervention in state and local taxation is broadly consistent with public choice theory; congressional abdication is overcome only by the public choice dynamics of concentrated benefits and disbursed costs). For a public choice perspective consistent with Moore's evidence and analysis see Jonathan R. Macey, *Federal Deference to Local Regulators and the Economic Theory of Regulation: Toward a Public Choice Theory of Federalism*, 76 VA. L. REV. 265 (1990).

201 The exertion of Congressional authority, moreover, would have to come in a crystalline fashion. *See, e.g., Mobil Oil Corp. v. Commissioner of Taxes of Vt.*, 445 U.S. 425, 448 (1980) ("Concurrent federal and state taxation of income, of course, is a well-established norm*. Absent some explicit directive from Congress*, we cannot infer that treatment of foreign income at the federal level mandates identical treatment by the States." (emph. added)); *Itel Containers Int'l Corp. v. Huddleston*, 507 U.S. 60 (1993) (inferring permission for a state tax from supposed congressional failure to issue explicit prohibition). Even in the foreign affairs context, where state power is at its nadir, state tax practice will stand barring an explicit congressional directive to the contrary. *Barclay's Bank, PLC v. Franchise Tax Bd*., 512 U.S. 298, 321-329 (1994) (lack of unambiguous indication of congressional intent to prohibit state tax regime constitutes implicit approval). The requirement of an explicit congressional preemption further narrows the room for legislative compromise and, hence, legislation over state taxation.

202 *See, e.g.*, *Quill Corp. v. North Dakota ex rel. Heitkamp*, 504 U.S. 298 (1992).

203 The origin of the modern Supreme Court's four-part dormant Commerce Clause test for state taxation, including the "fair apportionment" standard, is *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). For an overview of the Supreme Court's application of the test *see* Walter Hellerstein, Michael J. McIntyre, & Richard D. Pomp*, Commerce Clause Restraints on State Taxation After* Jefferson Lines, 51 TAX. L. REV. 47 (1995).

formula even if no other state in fact uses it.[204] Each state is thus free to adopt the formula that happens to maximize its own portion of the interstate tax take, with the result that taxation of more than 100 percent of some companies' income tax base is virtually a foregone conclusion. Even actual proof of double taxation, however, will not doom an individual state's apportionment scheme.[205]

Moreover, the Supreme Court tends to treat federalism cases brought by states more seriously and favorably than cases brought by private plaintiffs, who are likely to instrumentalize federalism arguments for unrelated purposes (such as profits).[206] Even the most flagrantly discriminatory state tax practice, however, will rarely be challenged by a victimized sister-state. A state that suffers from the use of a particular apportionment formula by another state will still hope to benefit from applying a different, though equally discriminatory, apportionment formula for its own benefit. In the *U.S. Steel* litigation, thirteen states—including some that had never joined the MTC, or joined and then left it, filed an *amicus* brief in defense of state authority.[207] No state argued against it. None could do so without undermining, in the process, its own authority over interstate taxation.

Having downplayed the manifest federal interests in interstate taxation in *U.S. Steel*, the Supreme Court itself felt compelled to safeguard those interests. Taking up, in

---

204 *See, e.g., Moorman Mfg. v. Bair*, 437 U.S. 267 (1978) (sustaining single-factor sales formula despite widespread adoption of three-factor formula).

205 *Container Corp. of America v. Franchise Tax Bd*., 463 U.S. 159, 187 (1983*); Barclay's Bank, PLC v. Franchise Bd*., 512 U.S. 298, 318-19 (1991) (actual double taxation does not violate dormant Commerce Clause unless it is the "inevitable" result of state's tax regime).

206 Cite

207 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452 (1978), Brief *amicus curiae*

the immediate aftermath of *U.S. Steel*, a series of cases involving ambitious state efforts to reach corporate subsidiaries under expansive notions of unitary taxation, the Justices valiantly, and with mixed results, struggled to hack their way through the thicket of corporate organization.[208] Those rulings at least had the advantage of conceding that interstate taxation did after all implicate federal (constitutional!) concerns—albeit, for reasons the Court did not bother to explain, not the sort of federal concerns that would trigger the congressional consent requirement under the Compact Clause. When the attempt to develop manageable constitutional rules proved unsuccessful, the Court effectively jettisoned it,[209] leaving corporations without protection against exploitative state taxation.[210]

In addition to the direct economic losses attendant to double taxation, the Court's *de facto* abandonment of the field produced a diplomatic crisis with America's closest allies and trading partners over the states' aggressive application of unitary taxation and worldwide combined income principles to foreign corporations doing business in the United States. Those corporations and their governments complained bitterly, through

---

[208] *See Exxon Corp. v. Wisconsin Dept. of Revenue*, 447 U.S. 207 (1980) and *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980) (sustaining state finding of "unitary business"); *ASARCO, Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307 (1982) *and F.W. Woolworth Co. v. Taxation and Revenue Dept*., 458 U.S. 354 (1982) (rejecting state findings and assessments).

[209] *Container Corp. of America v. Franchise Tax Bd*., 463 U.S. 159, 175 (1983) ("Court will, if reasonably possible, defer to the judgment of state courts in deciding whether a particular set of activities constitutes a 'unitary business.'") Although Justice Brennan, writing for the Court in *Container Corp.*, struggled mightily to paint this wholesale deference as consistent with the painstaking judicial scrutiny applied in preceding cases (*see, e.g., Container Corp*., 463 U.S. at 176 n. 15), it is not. The Supreme Court has over the past two decades largely ignored interstate tax problems, and its rare interventions have, with exceedingly rare exceptions (*e.g., Oklahoma Tax Comm'n v. Jefferson Lines, Inc*., 514 U.S. 175, 200 (1995)), been highly deferential. *Cf.* DANIEL SHAVIRO, FEDERALISM IN TAXATION 4 (1993) (lamenting Supreme Court's "wholesale retreat from even its limited past efforts in the area").

[210] State revenue departments will not find unitariness unless it means more revenue for the home team—which, in turn, means that state courts will rarely, if ever, upset such findings.

diplomatic and legal channels, about the states' tactics, which they—and, for the most part, the United States government—believed to contravene international tax treaties.[211] The long-running dispute was already brewing at the time of the *U.S. Steel* litigation; Justice White's dissent referenced it explicitly.[212] It was settled only well over a decade later, after much acrimonious litigation and diplomatic exertions.

While one can argue whether the Supreme Court's *U.S. Steel* decision or its Commerce Clause decisions wreaked more havoc, the central point—for present purposes—emerges with perfect clarity: the Court's own post-*U.S. Steel* decisions belie the contention that ordinary supremacy arrangements suffice to safeguard constitutional values in the area of interstate taxation. The most plausible vehicle of judicial intervention is the dormant or negative Commerce Clause[213]—which, in contrast to the Due Process Clause or the Equal Protection Clause, does not create irreversible constitutional commands. It operates rather like the Madisonian negative: it puts state regulation out of operation, pending a congressional decision to the contrary. The trouble, of course, is that "the 'negative Commerce Clause' … is 'negative' not only because it negates state regulation of commerce, but also because it does *not* appear in the

---

211 The foreign governments' long-running, progressively apoplectic complaints and the Executive's efforts to manage the diplomatic crisis are described, discussed, and shrugged off in Justice Ginsburg's majority opinion in *Barclay's Bank, PLC v. Franchise Tax Bd*., 512 U.S. 298, 324-331 (1994). For an account of the controversy, the *Barclay's Bank* litigation, and the resolution of the conflict *see* Edward T. Swaine, *Negotiating Federalism*, 49 DUKE L. J. AT 1159-61.

212 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 488-89 (White, J., diss.).

213 The dormant Commerce Clause is more appropriately called the "negative Commerce Clause." As Justice Thomas has quipped, there is nothing "dormant" about the Supreme Court's jurisprudence in that area: *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 609 n. 1 (1997) (Thomas, J. diss.)

Constitution."[214] Demanding constitutional tests under the Clause might curb exploitative state practices. But they tax judicial competence; threaten to constitutionalize essentially legislative judgments, such as tax apportionment formulas; and put enormous pressure on what is essentially a functional justification of a judge-made doctrine of questionable provenience.[215] More lenient dormant Commerce Clause tests are more readily justified, but they facilitate state practices that everyone, including the deciding Justices, knows to be discriminatory and exploitative.

Regardless of what one thinks of the legitimacy of the negative Commerce Clause and its proper scope and content, the same conclusion follows vis-a-vis the Compact Clause. A critique of the negative Commerce Clause as an "intellectual adverse possession"[216] surely cannot dismiss interstate exploitation as constitutionally irrelevant. Rather, it must contend that the Constitution exhaustively lists the means by which such exploitation must be fought.[217] Conversely, if concerns over interstate exploitation warrant a judicially created negative, they most certainly warrant the enforcement of the constitutional negatives—including the Compact Clause.

---

214 *Oklahoma Tax Comm'n v. Jefferson Lines, Inc*., 514 U.S. 175, 200 (1995) (Scalia, J., diss.) (emph. in original).

215 In recognition of these considerations, even advocates of comparatively stringent dormant Commerce Clause doctrines make do with tests that leave considerable room for state tax exploitation and discrimination. *See, e.g.*, DANIEL SHAVIRO, FEDERALISM IN TAXATION 95, 112-14 (1993); Jesse H. Choper & Tung Yin, *State Taxation and the Dormant Commerce Clause: The Object-Measure Approach*, 1998 SUP. CT. REV. 183, 211-12 *et pass*.

216 *Tyler Pipe Indus. V. Wash. State Dept. of Revenue*, 483 U.S. 232, 265 (1987) (Scalia, J.).

217 For a judicial argument along these lines *see Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 609 (1997) (Thomas, J. diss.) (urging enforcement of the Import-Export Clause, rather than the negative Commerce Clause, as the constitutional means of policing state invasions on interstate commerce).

E. Harmless Error?

Perhaps the best defense of the *U.S. Steel* decision is that the MTC's real-world effects are no big whoop. The argument comes in a political and in an economic version. Both possess a veneer of plausibility. Both, however, are untenable.

The political defense rests on the MTC's broad acceptance and modest role. Non-Compact states and business interests seem to have accommodated themselves to the MTC and the Commission.[218] While the Supreme Court's endorsement of the MTC may have further weakened Congress's will to tackle the state taxation of interstate business, that effect is probably marginal; one can argue with equal plausibility that the still-extant possibility of federal intervention has disciplined the MTC and its member-states. Serious quarrels over state taxation and conflicts with federal interests tend to be occasioned by actors other than the Commission. The driving force behind state unitary taxation and worldwide combined reporting, for example, was the California Franchise Tax Board,[219] and while the MTC may have spread and intensified state support for the Board's position,[220] California had adopted it long before the MTC's creation and would have pursued it in any event.[221] Similarly, relentless efforts to extend state use tax collection

---

[218] For example, the Council on State Taxation, a business trade association, promotes "equitable and nondiscriminatory state and local taxation" and cooperation with the MTC. http://www.statetax.org (visited Feb. 28, 2002).

[219] Jerome R. Hellerstein, *State Taxation Under the Commerce Clause: An Historical Perspective*, 29 VAND. L. REV. 335, 346 (1976); *Barclay's Bank, PLC v. Franchise Tax Bd.*, 512 U.S. 298, 306 (1994) (California "nearly the last state" to confine combined reporting to U.S. water's edge).

[220] Peters, *Use of Combined Reporting Required by Increasing Number of States*, 41 J. TAX. 375 (1974). The frequency of the Supreme Court's "unitary business" and apportionment cases in the years after *U.S. Steel*, as well as the fact that all of the state defendants in those cases were members of the MTC, suggest that the MTC played an independent or at least a catalytic role in the spread of those tax practices.

[221] Every cartel needs an exploitable advantage and, moreover, a leading member to enforce market discipline. California's exploitable advantage is its sheer size: no (multi-) national corporation can afford to withdraw from its huge market. While smaller MTC member-states from Kansas to North Dakota may

obligations to "remote" Internet or catalogue sellers—that is, sellers that have no nexus, such as a store, in the taxing jurisdiction—have been led by some state courts and, in the political arena, by the National Governors' Association and other state and local lobbying organizations. The MTC has played a subordinate, supporting role.[222]

But while these considerations might and probably should impress members of Congress in a hypothetical debate over the wisdom of approving the MTC, they beg the constitutional question of whether the protection against state compacts and their adverse effects can be left to the uncertain exercise of ordinary federal supremacy. The answer to that question is "no." The Founders adopted the Compact Clause precisely because the *ex post* exercise of supremacy is too uncertain and, as to compacts, too demanding.

On economic grounds, it can (and has) been argued that the risk of state cartelization is too minimal to warrant judicial insistence on the Compact Clause negative. State policy cartels face the same difficulties that confront every private cartel—holdout problems; disagreement over the distribution of gains from cooperation; and the risk of defection. Barring central political intervention and organization, cartels

---

collectively possess comparable market power, the risk of defection precludes them from asserting it. California alone can afford to push for worldwide unitary taxation (much as it can insist that Detroit manufacturers build cars exclusively for the California market). As a condition of its MTC membership, California insisted on a modification, in favor of populous states, of the one-state, one-vote regime specified in the Compact and, moreover, on the non-enforcement of certain Compact provisions. In light of California's importance to the functioning of the cartel, the MTC acceded to both demands. Sharpe, *State Taxation* at 246 n. 58, 272-73 n. 211. It may be only a slight exaggeration to describe the MTC as a multistate stage for the California Franchise Tax Board.

California's dominant position may in a sense seem to confirm the *U.S. Steel* Court's averment that the MTC confers no power that a single state could not exercise on its own, *see U.S. Steel Corp. v. MTC*, 434 U.S. 452, 472-73 (1978): as a practical matter, the Compact arguably confers no power that *California* could not exercise on its own. Exploitable advantages, however, raise difficult constitutional issues even when the exploitation is undertaken by individual states (*e.g.*, through severance taxes on natural resources). The constitutional minimum is that states must do the exploiting on their own—or else, obtain congressional consent.

222 *See, e.g.*, David Cay Johnston, *A Decisive Time in Fights Over Sales Tax*, N.Y. TIMES Dec. 18, 2000, C-10 (describing NGA's lead role).

ultimately cannot overcome these problems.[223] Thus, a Compact Clause that guards against unapproved state cartels guards against an exceedingly small and possibly non-existent risk.[224]

The MTC's history certainly illustrates the difficulties attendant to state cartelization. From the outset, the MTC confronted hold-out opposition from eastern domicile states and from states such as Arizona, whose income from copper mines could, under traditional allocation principles, be fairly attributed entirely to the state.[225] That pattern has continued to this day. Similarly, the MTC has proven incapable of solving distributional conflicts among its members. Theoretically, complete apportionment and unitary taxation can capture an enormous stream of income that would otherwise escape taxation (due to coordination problems, "leakage" and "evasion," and locational competition). That prospect prompted the formation of the MTC. But even if the prospective gains were to make every state better off (relative to the pre-existing regime of uncoordinated tax competition), they still generate disputes over their distribution. An apportionment formula that is neutral with respect to the pre-existing distribution of tax revenue would lock in, rather than eviscerate, locational competition. It is therefore unacceptable to the market states that stand to gain most from cartelization. (Conversely, an apportionment formula that changes the pre-existing distribution will generate the

---

223 Albert Breton, *The Existence and Stability of Interjurisdictional Competition*, *in* COMPETITION AMONG GOVERNMENTS 49 (Daphne A. Kenyon & John Kincaid eds., 1991). Consistent with this prediction, some states anticipated the need for central intervention as a prerequisite for effective state tax cartelization. In the early 1970s, for example, an ad-hoc group of state officials and business leaders proposed federal legislation that would enable the MTC to make binding decisions for all fifty states. Sharpe, *State Taxation* at 266-67 n. 172. That proposed compromise between state autonomy and national uniformity, however, was never acted upon.

224 Note, *To Form a More Perfect Union? Federalism and Informal State Cooperation*, 102 HARV. L. REV. 842, 860-61 (1989).

aforementioned hold-out problems.) This baseline problem has no technocratic solution, for no apportionment formula is neutral.[226] For this reason, few if any MTC regulations are truly uniform; their application and interpretation in the member-states vary greatly. The inability to agree on a neutral baseline, in turn, means that the MTC must make continuous decisions that affect the distribution of apportioned tax income—an institutional feature that further increases the risk of hold-outs and defections.[227] The MTC has been compelled to minimize those risks by disavowing any power to make binding decisions for the member-states. The Commission can cajole recalcitrant members (other than California), and it can advance its "recommendations," in cooperation with state officials, by exploiting agency and monitoring problems at the state level.[228] But it cannot truly enforce any particular market order, even on its members.

Even so, the predictable failure of the MTC or for that matter of most state cartels to live up to their aspirations provides no good reason to refrain from enforcing the Compact Clause. Some state cartel might succeed in exploiting their advantages to a troublesome extent. (The tobacco tax cartel, to be examined shortly, is a clear example.) Thus, even if state cartelization is an insubstantial risk, it is still *a* risk. Judges are poorly equipped to determine, through a case-by-case examination of individual compact-

---

225 Sharpe, *State Taxation* at 271.

226 For instance, the distribution of apportioned income under a commonly used three-factor formula (property, payroll, and sales) will favor states with high property values in direct proportion to the relative weight given to that factor.

227 Sharpe, *State Taxation* at 271. ("[W]hat [holdout] states really fear is an organization with the power to *continually* make judgments that are binding on them.")(emph. in the original).

228 *See infra* nn. and accompanying text.

cartels, just how much cartelization is too much, or whether a particular state cartel might wield more or less market power in the future. Similarly, one can imagine some efficient state cartels; the cooperative management of a common pool (such as fisheries) through quotas may be an example. What looks like sustainable yield management to some, however, will look like a naked output restriction to others. A judicial inquiry into the purpose of the cartel arrangement will be a crapshoot, and the allocation and distribution of its costs and benefits are essentially a political judgment. All told, we are better off with a per se rule that commits the approval or rejection of state cartels to the Congress.

The functional argument for a lenient Compact Clause interpretation is that a judicial insistence on the congressional negative would thwart potentially beneficial state agreements, without averting any serious risk. That argument, though, cannot apply to policy cartels, for the promised benefits—harmonization and coordination—are merely the flipside of the cartel risk. If the risk is negligible (on account of the difficulties attendant to effective cartelization), the corresponding benefits, if any, are too small to justify a latitudinarian Compact Clause interpretation. Conversely, if the prospective benefits of spontaneous state coordination and harmonization are deemed large, then so is the cartel risk. Either way, the argument collapses under its own weight.

VI. The Multi-State Settlement Agreement on Tobacco Litigation

The November 1998 Multistate Settlement Agreement (MSA) provides for a comprehensive settlement of then-pending state lawsuits against the major U.S. tobacco manufacturers. The core provisions of the MSA obligate the participating tobacco

manufacturers to pay very substantial sums, estimated at roughly $206 billion through the year 2025,[229] to the 46 signatory state governments.[230] In addition, the MSA establishes a massive regulatory regime governing the sale and marketing of tobacco products in the United States.

The MSA differs in several salient respects from any preceding interstate agreement, actual or contemplated. First, the Agreement aids none of the purposes that have traditionally served to justify a latitudinarian interpretation of the Compact Clause. The agreement does not respond to a regional problem that had escaped the attention of the Congress; it responds to a national problem and regulates a national industry. Some aspects of tobacco marketing (such as advertising) had been the subject of federal legislation and regulation for a considerable period of time. Nor does the agreement even purport to redress problems of scale, interstate externalities, or coordination that might affect the state regulation and taxation of tobacco. Purported "race to the (anti-regulation) bottom" problems do not affect the regulation of the consumption and marketing of cigarettes.[231] State competition does of course affect the taxation of tobacco products, and as shown below, the MSA payments are structured as a uniform national tax so as to prevent cross-border arbitrage and tax leakage. It would be hard to argue, however, that

---

229 Hanoch Dagan & James J. White, *Governments, Citizens, and Injurious Industries*, 75 N.Y.U.L. REV. 354, 372-73 (2000) (hereafter Dagan & White, *Injurious Industries*). The financial provisions of the MSA are briefly described *infra* nn. and accompanying text. For an overview see W. Kip Viscusi, *A Postmortem on the Cigarette Settlement*, 29 CUMB. L. REV. 523, 537-43 (1999).

230 The government signatories also include five territories and the District of Columbia. For reasons of convenience, I will simply refer to "states."

231 Except perhaps in very extreme cases (such as complete local prohibition), smokers are unlikely to sort themselves in accordance with state or local smoking restrictions, let alone advertising regulations. The proliferation of restrictions over the past few decades belies any "race to the bottom" theory. *See* MARTHA DERTHICK, UP IN SMOKE: FROM LEGISLATION TO LITIGATION IN TOBACCO POLITICS 21-24 (2002) (hereafter DERTHICK, UP IN SMOKE).

individual states are incapable of taxing tobacco products. Over the two decades preceding the MSA, state and local tobacco taxes increased on average, and differences in state tax rates widened substantially.[232]

Second, the MSA is the first interstate compact to which private market actors—tobacco manufacturers—are an official party. Producer cartels in the guise of interstate agreements are not unprecedented; the (congressionally approved and later dismantled) Interstate Oil Compact is an example.[233] The MSA, however, is the first compact that constitutes both an agreement among the states and a legally binding agreement between the states and a specific group of producers (the originally participating manufacturers).

These observations point to the MSA's third distinctive feature: it constitutes a cartel in the most pristine sense. The Multistate Tax Compact is a "cartel" in the sense that it seeks to displace policy competition—in other words, in the same sense in which most state or supra-state regulation constitutes cartelization. The MSA, in contrast, establishes an actual market cartel. Its convoluted provisions insulate the participating manufacturers from competition by new market entrants and, short of a tipping point at which price elasticities reduce tobacco consumption, ensure that consumers will pay

---

232 Kathy Kristof, *Border Crossers Sometimes Can Save a Fortune on Exise Taxes*, DALLAS MORNING NEWS July 13, 1997, 3-H (citing expert estimates and studies).The widening range of state tax rates generated substantial increases in cross-border purchases and smuggling, also known as "buttlegging." Id. While neither producers nor state governments welcome those effects, the increased divergence of state policies over time belies any notion of a "race to the bottom" that deprived the states of autonomous policy choices. Congress had proven willing to address the buttlegging coordination problem: *see, e.g.,* Contraband Cigarette Act, P.L. 95-575, 92 Stat. 2463 (1978) (codified at 18 U.S.C. 2341 et seq. (1994). The MSA made no provision in that regard and may in fact have exacerbated the problem. Michael Beebe, *Seneca Indians Sending Electronic Smoke Signals Over the Internet*, BUFFALO NEWS Dec. 12, 1999, 1-A. The notion of the MSA as a response to collective action problems and unresponsiveness on the part of national institutions is a canard. DERTHICK, UP IN SMOKE AT 212-18.

233 *See supra* nn. and accompanying text.

virtually all of the costs associated with the MSA.[234] The "damages" paid under the MSA represent the states' share of the difference between the market price and the monopoly price.

Fourth, the MSA is one of only a handful of state agreements to be joined by all, or very nearly all, states. Since the entry of the agreement, moreover, no state has revoked its participation or demanded a significant revision of its terms. The architects of the MSA, in other words, found an effective mechanism to combat the holdout and defection problems that ordinarily bedevil state cartels. That mechanism is the deliberate imposition and exploitation of the interstate externalities against which the Compact Clause is meant to protect states and their citizens.[235]

---

[234] Dagan & White, *Injurious Industries* , 75 N.Y.U. L. REV. at 382; Michael DeBow, *The State Tobacco Litigation and the Separation of Powers in State Governments: Repairing the Damage*, 31 SETON HALL L. REV. 563, 569 (2001) (consumers will pay roughly 90 percent of the cost of the MSA (citing interview with W. Kip Viscusi)). Price increases immediately followed the announcement of the MSA. *Id.*

[235] Arguably, the MSA's manifest conflict with the Compact Clause is the least of its problems. Legal scholars and political scientists have harshly criticized the collusive and, in some instances, corrupt relations between the private plaintiffs' attorneys and state attorneys general who instigated the state lawsuits against tobacco manufacturers (*see, e.g.*, Margaret A. Little, *A Most Dangerous Indiscretion: The Legal, Economic, and Political Legacy of the Government's Tobacco Litigation*, 33 CONN L. REV. 1143, 1150-56 (2001); the legislative abrogation in some states of the tobacco companies' common law defenses during the pendency of the state lawsuits, (*id.* at 1147); and the symbiotic relationship between state governments and the participating manufacturers that has resulted from the MSA (*see, e.g.,* Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 378-81). Critics have further described the state lawsuits as essentially baseless, (*see, e.g.*, Michael DeBow, *The State Tobacco Litigation and the Separation of Powers in State Governments: Repairing the Damage*, 31 SETON HALL L. REV. 563 (2001); Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 354, 360-62); objected to the MSA on antitrust and economic grounds (*see, e.g.*, and Jeremy Bulow & Paul Klemperer, *The Tobacco Deal*, BROOKINGS PAPERS ON ECONOMIC ACTIVITY: MICROECONOMICS 323 (1998); Thomas C. O'Brien*, Constitutional and Antitrust Violations of the Multistate Tobacco Settlement* 9 (CATO INSTITUTE POLICY ANALYSIS No. 371, May 2000)); and described the MSA as inconsistent with the basic principles of representative government (*see, e.g.*, Jonathan Turley, *A Crisis of Faith: Tobacco and the Madisonian Democracy*, 37 HARV. J. ON LEGIS. 433 (2000); DERTHICK, UP IN SMOKE). *See also* further references cited throughout this Part. In light of this litany, an insistence that the MSA also violates (of all things) the Compact Clause may seem pedantic. If so, the discussion may serve as a reminder that structural constitutional provisions, including such arcane provisions as the Compact Clause, often help to prevent big, unmanageable political problems—so long as they are enforced.

A. The MSA: A Brief History

The first state lawsuit against tobacco manufacturers was filed in 1994, at the suggestion of an anti-tobacco trial lawyer (and subsequently with his cooperation) by Mississippi's enterprising Attorney General, Michael Moore.[236] The lawsuit included, *inter alia*, a claim for recovery of Medicaid costs allegedly attributable to smoking. Moore lobbied other state attorneys general to file similar recoupment cases. By mid-1997, 31 states had followed suit. These copycat suits alleged liability on a number of theories, including (in most cases) Medicaid recoupment, consumer fraud, antitrust violations, unjust enrichment, and violations of state consumer protection laws. Democratic attorneys general were much faster to sue than Republicans.[237] Major tobacco-manufacturing states (Virginia, North Carolina, Kentucky, and Tennessee) refrained from filing, as did Delaware and Wyoming.

Mississippi's lawsuit settled for $3.6 billion in July 1997; Florida's case settled a month later for $11.3 billion. At that stage, adverse developments—in particular, the defection of the Liggett Company, a particularly vulnerable tobacco producer, and the legislative abrogation of common law liability defenses in such states as Florida and Maryland—had already induced the tobacco companies to sue for peace. In June 1997, tobacco lawyers, plaintiffs' attorneys, and attorneys general met in Washington, D.C. to hammer out a comprehensive agreement, known as the "Resolution." A precursor to the

---

[236] The history of state tobacco litigation has been told often and well. *See, e.g.*, PETER PRINGLE, CORNERED: BIG TOBBACCO AT THE BAR OF JUSTICE (1998); CARRICK MOLLENKAMP ET AL., THE PEOPLE VS. BIG TOBACCO (1998); MICHAEL OREY, ASSUMING THE RISK (1999); DAN ZEGART, CIVIL WARRIORS (2000); and most recently DERTHICK, UP IN SMOKE. Unless otherwise referenced, the account in the text follows Derthick's narrative.

[237] More than two years passed before the first Republican attorneys general (of Kansas and Arizona) followed Mississippi's lead. DERTHICK, UP IN SMOKE at 79.

MSA, the Resolution provided for a comprehensive financial settlement, projected to amount to $368.5 billion over 25 years,[238] of all pending state lawsuits, in return for expansive protections against civil liability (including bars to class action lawsuits, punitive damages in individual tort suits, and addiction claims) for the settling manufacturers.[239] The Resolution would also have conferred authority on the federal Food and Drug Administration to regulate nicotine, the active ingredient of tobacco, as an addictive drug.

The parties then submitted the proposed federal legislation to Congress. Under the leadership of Senator John McCain (R-AZ), then-Chairman of the Senate Commerce Committee, a bill based on the Resolution—but containing provisions for substantially higher industry payments and more limited liability protections—was debated and eventually reported to the Senate floor. In June 1998, however, the bill died after a failed cloture vote. The prevailing—though not uncontested—explanation for the failure is that anti-tobacco and public health advocacy groups, unwilling to brook a compromise with tobacco companies, had loaded the compromise Resolution with provisions that proved unacceptable to the industry.[240] (The version of the bill that was reported out of the Senate Commerce Committee stipulated industry payments in the amount of $516 billion, and the civil liabilities provisions contained in the Resolution and earlier committee drafts had been dropped.)[241] In a massive advertising campaign that may have had a

---

238 Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 364-65.

239 *Id.* at 365-66.

240 DERTHICK, UP IN SMOKE 130-146, provides a balanced discussion of the factors that contributed to the failure of the proposed legislation.

241 Dagan & White, *Injurious Industries*, 75 N.Y.U.L. REV. 354, 367.

certain "bounce" on Capitol Hill,[242] the industry portrayed the bill as a tax hike and a boondoggle for trial lawyers, rather than a public health measure.

As the prospects for a federal enactment dimmed, nine state attorneys general—chosen to represent a spectrum of regions, degrees of hostility to the industry, and stages of progress in the lawsuits[243]—met in secret negotiations with trial lawyers and industry representatives to work out an agreement along the lines of the Resolution, though more moderate in scope.[244] In November 1998, the parties reached an agreement. Total industry payments to the settling states were reduced to roughly $206 billion by 2025. Provisions for the FDA regulation of tobacco products, which obviously would have required federal approval and legislation, were stripped.[245] Likewise, the expansive civil liability limitations contained in the Resolution were jettisoned and replaced with narrower protections from state-initiated lawsuits against the industry.

The MSA was released on November 14, 1998, and all 46 state attorneys general promptly approved it. Four non-participating states (Mississippi, Florida, Texas and Minnesota) had reached earlier agreements with the industry (totaling $40 billion), which

---

242 DERTHICK, UP IN SMOKE at 122-23.

243 *Id.* at 171.

244 For a useful comparison of the major provisions of the Resolution, the Senate bill, and the MSA see Dagan & White, *Injurious Industries*, 75 N.Y.U.L. REV. 354, 364-73.

245 *Food & Drug Administration v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000) (FDA lacks statutory authority to regulate tobacco). While the Supreme Court's ruling of course postdates the MSA, the Fourth Circuit Court of Appeals' ruling in the same case, to the same effect, issued in August 1998, during the negotiations over the MSA. *Brown & Williamson Tobacco Corp. v. Food & Drug Administration*, 153 F.3d 155 (4th Cir. 1998), *aff'd*, 529 U.S. 120 (2000). While affirmance was not a foregone conclusion, the MSA negotiators were not so bold as to contrive to confer upon a federal agency, without the consent of the Congress, a regulatory authority that the agency may or may not have possessed.

were preserved under the MSA. The MSA was not presented to the Congress for approval.

B. The Structure of the MSA

In pending litigation over the MSA, defendants (participating manufacturers and states) have averred that the MSA does not constitute an "agreement or compact" among the states at all.[246] Rather, they insist, since the MSA must under its terms be implemented through a consent decree in each participating state's courts,[247] it constitutes nothing but a settlement of the lawsuits brought by each individual state against the tobacco companies. It just so happens that the defendants and the terms of settlement are the same in each case and state.

This hyper-technical argument is difficult to understand as anything but a joke. The MSA bears the signatures of state attorneys general who never filed, let alone prosecuted, a case against the defendants. Putting that aside, and further ignoring that even the *U.S. Steel* Court declined to grant a Compact Clause exemption based on mere formalities,[248] the MSA bears the "classic indicia" of a state compact even in the narrowest sense of that term.[249] The MSA establishes, authorizes, and funds several joint

---

246 *See Star Scientific v. Beales*, 278 F.3d 339, 360 (4th Cir. 2002) (briefly discussing and rejecting that contention).

247 MSA II (ss) ("state-specific finality"); Exhibit L.

248 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 470-71 (1978) ("[T]he mere form of interstate agreements cannot be dispositive… The [Compact] Clause reaches both 'agreements' and 'compacts,' the formal as well as the informal.").

249 *Cf.. Northeast Bancorp, Inc. v. Bd. of Governors of the Federal Reserve*, 472 U.S. 159, 175 (1985) (describing some of the "classic indicia" of a compact: establishment of a joint body; conditional action by other states and bar to unilateral modification or repeal; and mandatory reciprocity).

bodies for the administration and legal defense of the Agreement.[250] Unlike the earlier Resolution, the MSA divides a stream of industry payments among the participating states in accordance with an agreed-upon formula described in the Agreement,[251] an arrangement that looks very much like an agreement among the states.[252] Under its terms, the MSA cannot be fully implemented without entry of consent decrees by state courts representing 80 percent of the number of states and of the aggregate payment allocations specified by the Agreement.[253] Receipt of the proceeds requires performance of specific duties by the settling states, including, but by no means limited to, entry of the MSA by a state court.[254] Withdrawal from the Agreement or failure to perform specified obligations—such as the enactment of a state model statute subjecting non-participating tobacco manufacturers to taxation—carries severe financial penalties, which are

---

[250] *See* MSA VIII(c) (funding for the enforcement and implementation of the MSA through the National Association of Attorneys General (NAAG)); MSA VI (establishment of a national foundation, under the auspices of the NAAG and other state organization, for certain purposes); MSA IX (d)(2)(G) (authorizing private consulting group, ominously named "The Firm," to make "conclusive and binding" legal and financial determinations concerning payment allocation).

[251] MSA Exhibit A. The Resolution contained no distribution formula: Dagan & White, *Injurious Industries,* 75 N.Y.U. L. REV. at 364-65, 373

[252] Industry payments are made, not to individual states but into an Escrow Fund under the administration of independent third parties. MSA IX (a). So long as the participating manufacturers make the appropriate aggregate payments, disputes over the distribution are entirely among the states. Such disputes are subject to mandatory arbitration, MSA XI (c).

[253] MSA II (u). The original participating manufacturers may waive the requirement for final approval by unanimous written consent. *Id.*

[254] *See, e.g.*, MSA VII (Enforcement); IX (d)(2) (enactment, diligent enforcement, and full legal defense of "Qualifying Statute" that "effectively and fully neutralizes the cost advantages that the Participating Manufacturers experience vis-à-vis Non-Participating Manufacturers," IX (d)(2)(E)); XII (a) (mandatory releases); XIII (consent decree and dismissal of claims); XVIII (l) (best efforts to cause Agreement to become effective).

enforceable by the states that remain under the MSA's umbrella.[255] Amendments require the consent of all affected states and participating manufacturers.[256]

Most important for Compact Clause purposes, the central purpose of the MSA, the establishment of a national producer cartel and the distribution of the surplus proceeds to state governments, could not be accomplished without concerted state action. About the centrality of that purpose, the MSA leaves no doubt. There are a lot of bells and whistles, ranging from lobbying restrictions on tobacco manufacturers[257] to document disclosure mandates[258] to advertising and marketing regulations, all the way down to Joe Camel and the Kool Jazz Festival.[259] But the financial terms form the hard core of the MSA. Those terms restrict market entry, suppress price competition within the industry, and ensure that the manufacturers' payment obligations are passed on to consumers.[260]

In order to meet their payment obligations under the MSA, the four "original participating manufacturers" who, at the time, accounted for close to 99 percent of the U.S. cigarette market, had to increase prices. Since price competition would have

---

255 MSA IX (d)(2); XVIII (g) ("Each Settling State and each Participating Manufacturer hereby represents that this Agreement … will constitute a valid and binding contractual obligation, enforceable in accordance with its terms, of each of them.").

256 MSA XVIII (j). Certain portions of the MSA are amendable by unanimous consent among the states, without the manufacturers' participation. MSA IX (f)(6).

257 MSA III (m)-(r).

258 MSA IV.

259 *See, e.g.*, MSA III (a)-(j), II (l).

260 The following paragraphs describe the principal payment obligations stated in MSA IX, which account for an overwhelming portion of the total settlement amount. The MSA contains additional payment obligations concerning, *inter alia*, the establishment on a national anti-tobacco research foundation MSA VI; contributions to the NAAG's legal defense and MSA enforcement fund, MSA VIII c; and plaintiffs' attorneys' fees, MSA XVII.

precluded the requisite, dramatic price increase (of some 35 cents per pak),[261] the MSA allocates the manufacturers' share of the payments in proportion to current market share. A higher market share means higher "damage" payments, rendering price competition for a higher market share futile. In order to protect the original participating manufacturers against new market entrants, the MSA provides non-participating manufacturers with an incentive to join the MSA without incurring proportionate payment obligations—provided, however, that those small manufacturers agree to stabilize their sales at pre-MSA levels.[262]

For the regulation of producers who refuse to accept that bargain and for the suppression of new market entrants, the MSA imposes a regime of interstate transfer payments. If the participating manufacturers suffer sales losses exceeding two percent of their aggregate market share, they may reduce their base payments to the states by three percent for each percent market share loss above that level.[263] In other words, a 10 percent decline in aggregate market share entitles the participating manufacturers to a 24 percent reduction in (adjusted) base payments to the states. Any state may, however, escape an adjustment by enacting a model statute, contained in Exhibit O to the MSA, which "fully and effectively neutralizes" the participating manufacturers' cost disadvantages attributable at the MSA.[264] While new market entrants have by definition caused none of the damages that the MSA is supposed to redress, the MSA Model Statute requires them to make payments, equivalent to roughly 150 percent of the "damage"

---

261 Bulow & Klemperer, *The Tobacco Deal* at 376-77.

262 MSA IX (i).

263 MSA IX (d)(1).

264 MSA IX (d)(2)(E); Exhibit T.

payments they would incur under the MSA itself, into an escrow account, supposedly in anticipation of future costs and liabilities.[265] Should the aforementioned market share losses among the participating manufacturers still occur, the participating manufacturers' payment reductions will be imposed on states that have failed to enact and enforce the model statute or an equivalent qualifying statute. Such states may lose their entire allocable share. Enacting states whose model statutes are struck down by a court may still lose up to 65 percent of their allocable shares.[266] Due to these "diabolically clever"[267] provisions and incentives, virtually all states have enacted a model or qualifying statute.[268]

C. Compact Risks

Among the state compact risks identified earlier (cartelization, agency problems, externalities, and invasions of federal supremacy), one need not long detain us: in purpose and effect, the MSA is a naked cartel. The MSA's effects on sister-state interests, political accountability, and federal supremacy are marginally more subtle, but no less egregious.

---

265 MSA Exh. T Sec. 1 (f); Sec. 3 (b).

266 MSA IX(d)(2)(F). Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 381-82.

267 Dagan & White, *Injurious Industries*, 75 N.Y.U.L. REV. 354, 381.

268 The restrictions on market entry have proven not entirely effective; during the MSA's operation, the market share of non-participating manufacturers has risen to over four percent. Gordon Fairclough, *Competition for Cheap Smokes Heats Up*, WALL STREET JOURNAL Feb. 15, 2000, B-1. and "The Firm" has adjusted the states' base payments accordingly. Considering the states' and the manufacturers' enormous stakes in the MSA's preservation, however, far more dramatic inroads into the cartel are needed to induce conflicts that might endanger the arrangement.

Cartelization. An agreement in pursuit of the MSA's ostensible purposes—punishment for past corporate misconduct, redress for past harms, the procurement of public health gains through future smoking reductions—would be structured very differently. For example, such an agreement would aim to capture manufacturers' profits, instead of protecting them. It would facilitate and encourage state action adverse to tobacco interest, instead of giving states a direct financial stake in the viability and financial health of four individual tobacco companies.[269] It would reflect some correspondence between individual defendants' past misconduct and their liabilities, and it would ensure that the proceeds are put to uses related to past and present injuries. The MSA payments, in contrast, are only tangentially (and, in the case of non-participating manufacturers, not at all) related to past misconduct,[270] and they flow into the states' treasuries as general receipts.[271] Notwithstanding their designation as "damages," the MSA payments bear no resemblance to a damage payment that might settle a suit in tort or equity. [272] They act like a uniform (and perpetual) national tobacco sales tax. And in order to ensure that the tax will be paid by consumers, the MSA cartelizes the tobacco market.

---

269 DERTHICK, UP IN SMOKE 221.

270 Bulow & Klemperer, *The Tobacco Deal* at 378-79 (manufacturers' market share is a highly inaccurate proxy for past damages).

271 Dagan & White, *Injurious Industries*, 75 N.Y.U.L. REV. 354, 372. The vast majority of states are using only a very small portion of settlement payments for tobacco prevention purposes. *See* www.tobaccofreekids.org/reports/settlements/2002/appendixb.pdf (visited Mar. 4, 2002).

272 Dagan & White, *Injurious Industries* , 75 N.Y.U. L. REV at 426-28; DERTHICK, UP IN SMOKE at 177 ; O'Brien, *supra* n. , at 2.

The MSA cartel, in short, is not a wolf in sheep's clothing; it is a wolf in wolf's clothing.[273] Had tobacco manufacturers contrived to establish a comparable arrangement without the states' collusion, their agents and officers might all be in jail.[274] All serious analysts of the MSA agree on its cartel nature,[275] and even the MSA's architects do not dispute that characterization: their defense of the MSA against that charge rests on the state action exemption to the antitrust laws and the related *Noerr-Pennington* doctrine.[276]

The state action doctrine may render the MSA—in Professor Ayres fitting description—"not clearly illegal" for antitrust purposes.[277] State action, however, and especially state action of a cartelizing, exploitative nature, is what the Compact Clause

---

273 "[T]his wolf comes as a wolf." *Morrison v. Olson*, 487 U.S. 654, 699 (1988) (Scalia, J., diss.). The perfect fit between Justice Scalia's fabulous phrase and the MSA has also occurred the plaintiffs' attorneys challenging the MSA. *See Star Scientific v. Beales*, 278 F.3d 339, 361 (4th Cir. 2002) (quoting plaintiffs' brief). The Fourth Circuit panel rejected the wolf-as-a-wolf contention (advanced by plaintiffs under a due process and an equal protection theory), substantially on the grounds that any measure that sails under an anti-tobacco label—including an arrangement that confers monopoly profits on purported "defendants" and hammers their competitors—must *ipso facto* be rational.

274 *See* Sherman Act, 15 U.S.C. 1 (criminalizing conspiracies in restraint of trade); FTC/DOJ Guidelines Antitrust Guidelines for Collaborations Among Competitors, sec. 3.2., *reprinted in* 4 TRADE REG. REP. (CCH) sec. 20 (2000) (defining "hard core cartel agreements" to be prosecuted criminally without regard to "claimed business purposes, anticompetitive harms, procompetitive benefits, or overall competitive effects").

275 *See, e.g.*, Bulow & Klemperer, *The Tobacco Deal* at 324; Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 425; Christopher Schroeder, *The Multistate Settlement Agreement and the Problem of Social Regulation Beyond the Power of State Government*, 31 SETON HALL L. REV. 612, 613-14 (2001); O'Brien, supra n. xx; Ian Ayres, *Using Tort Settlements to Cartelize*, 34 VAL. U. L. REV. 595 (2000) (hereafter Ayres, *Tort Settlements*).

276 *See,* respectively, *Parker v. Brown,* 317 U.S. 341 (1943); *California Retail Dealers Ass'n v. Midcal Aluminum,* 445 U.S. 97, 105 (1980) (state action doctrine); *and Eastern Railroad Conference v. Noerr Motor Freight*, 365 U.S. 127 (1961*); United Mineworkers of America v. Pennington*, 381 U.S. 657 (1965) (limited antitrust immunity for mere attempts to influence the enactment or enforcement of laws). The applicability of the doctrine to the MSA has been questioned by commentators, *see* O'Brien, *supra* n. at 12-14, and by anti-MSA litigants, albeit to date largely without success. *See, e.g., PTI v. Philip Morris*, 100 F.Supp.2d 1179 (C.D.Ca. 2000); *Bedell v. Philip Morris*, 263 F.3d 239 (3rd Cir. 2001) (finding defendants immune under *Noerr-Pennington* doctrine but not state action doctrine).

277 Ayres, *Tort Settlements*, 34 VAL. U. L. REV. at 598.

targets. That does not render the MSA clearly illegal. It does, however, render it illegal without congressional consent.[278]

Agency Problems. Tobacco policies vary enormously from state to state and even among local jurisdictions. There is an obvious difference between the smoke-filled diners of rural Tennessee and the suburban Maryland counties that regulate prohibit smoking in restaurants and even in public outdoor areas. Excise and sales taxes on cigarettes range from 2.5 cents in Virginia to $1.11 in New York—an astonishing range, considering the ease with which many consumers can evade sales taxes.[279] These policy differences reflect deep-seated political and cultural variations, as well as different economic interests (such as the importance of tobacco farming and production in some states). In all other policy areas, including areas where collective action problems are real and state coordination would yield substantial benefits (such as insurance regulation), far smaller state-to-state differences have consistently proven insurmountable. The obvious question is how the states, accustomed though they are to a prickly insistence on state sovereignty and to the defense of parochial interests, could possibly agree on a uniform scheme to tax and regulate tobacco sales and consumption.

---

[278] The point will appear particularly compelling to those who tend to the view (including, unsurprisingly, this author) that the antitrust state action doctrine itself should be confined, against the constitutional background, to state cartels whose costs fall principally on in-state residents, whereas state cartels that exploit non-citizens should not enjoy such protection. The classic formulation of this view is Frank Easterbrook, *Antitrust and the Economics of Federalism*, 26 J. L. & ECON. 23 (1983). *See also* Levmore, *Interstate Exploitation*, 69 VA. L. REV. at 626-629. The Compact Clause analysis expounded here and in Part IV, *supra*, is fully consistent with this perspective: if states gang up for exploitative purposes, we need not wait for courts to get antitrust (or for that matter the negative Commerce Clause) right; the likelihood of damage is so high that the Constitution calls for congressional review *ex ante*. Levmore, *id*. at 570 n. 17.

[279] DERTHICK, UP IN SMOKE 163 (citing year 2000 figures).

The answer lies in the structure of the MSA payment provisions as a national sales tax. Consumers in each state will pay the tax regardless of whether or not their state joins the MSA. Since states can opt out of the receipts but not the taxes, a non-participating state would simply leave "its" share of the MSA proceeds on the table and available for distribution to the participating sister-states.[280] Hence, the manifest political differences among the states affected only the timing of the states' participation and the degree of enthusiasm with which the attorneys general joined the campaign. Unanimity was a foregone conclusion once the first few states had made their move.

"Agency problem" does not begin to describe the difficulties with this policy-making process. The eventual drafting of the MSA and the establishment of a national producer cartel, conducted in secret negotiations between industry representatives, trial lawyers, and a handful of selected state attorneys general, should give pause.[281] More troublesome still, the dynamics of the MSA left the citizens of many states, and their elected officials, effectively without any voice. In the early stages of the state tobacco litigation, Alabama's attorney general refused to file a lawsuit in his state, sharply criticized the legal theories on which the lawsuits in other states were based, and argued vociferously against a comprehensive settlement.[282] In the end, he, too, signed the MSA. At that stage, Alabama's position no longer made a difference with respect to the

---

280 DERTHICK, UP IN SMOKE 163-73 and esp. 172 (identifying nation-wide imposition of MSA costs as the cause of state unanimity); William Pryor, *Actions and Multigovernment Lawsuits*, 74 TULANE L. REV. 1885, 1911 (2000) (Alabama Attorney General citing imposition of share of MSA costs on Alabama as reason for signing MSA despite his grave misgivings).

281 *See infra* n. and source cited *id.* (describing secret MSA negotiation). In a gilded but less jaded age, the considerably more transparent and arms-length interactions between national trusts and federal legislators were the stuff of raised eyebrows, presidential elections, and scathing cartoons.

282 William Pryor, *The Law Is at Risk in Tobacco Suits*, WALL ST. J. Apr. 7, 1997; *Actions and Multigovernment Lawsuits*, 74 TULANE L. REV. 1885 (2000).

collective policy choice and the attendant cost for (tobacco-consuming) Alabama citizens; the only question was whether or not the state should accept a proportionate share of the proceeds. The agency problem, in other words, is not that the MSA drove a wedge between the citizens of Alabama and their elected official.[283] The problem is that Alabama citizens' choice was made for them by the attorneys general of neighboring Mississippi and far-away Minnesota and Massachusetts.

Arguably, dissident states did still have a voice. Under its terms, the MSA requires the assent of eighty percent of the states, representing eighty percent of the allocable payment shares, to take full effect. Thus, a fairly small number of states, acting in concert, could have thwarted the deal. Any such concerted action, however, could have been thwarted by the participating manufacturers' unilateral waiver of the eighty-percent requirements,[284] and in any event, an anti-settlement coalition would have encountered insurmountable coordination and defection problems. The dynamics that produced the MSA thus provide occasion for another swipe at an already-rejected argument for a latitudinarian Compact Clause jurisprudence—to wit, the notion that the Compact Clause negative is unnecessary because collective action problems provide adequate protection against state cartels.[285] Unpersuasive, to my mind, even in settings where collective action problems do impede state collusion to the detriment of sister-states, the argument

---

[283] Circumstantial evidence suggests that the official champions of the state anti-tobacco campaign, rather than the opponents, may have acted at variance with their constituents' preferences. Opinion polls in Mississippi—the first state to file suit—indicated public opposition to such a lawsuit, and the state's attorney general filed the case in an equity court so as to avoid a trial by jury. DERTHICK, UP IN SMOKE 75-76. The attorneys general of Minnesota and Massachusetts, who had vigorously championed the lawsuits, lost their subsequent bids for the Governor's offices in their states; Mr. Pryor, who had fiercely resisted the lawsuits, was returned to his position as Alabama's Attorney General. *Id.* at 225-26.

[284] MSA II (u)(2).

cannot apply when collective action dynamics facilitate, rather than forestall, state-sponsored cartels.

Externalities. In principle, one can envision an uncoordinated state-by-state decisionmaking process that would produce a financial result comparable to the MSA: each state could impose an equivalent sales or excise tax on purchases within its borders. Alternatively, each state could sue manufacturers and settle on terms that impose the costs of the "damages" entirely on consumers within the state. To pose the hypothetical, however, is to reject it. Many states would refrain from taxing or suing at all; others might try and fail. Under those circumstances, neither the producer-defendants nor the states would be able to control private price arbitrage at the borders. The costs of the MSA payments, in contrast, are imposed uniformly and nationwide. Instead of replicating a series of internal settlements that each state could have obtained on its own, the state lawsuits generated a stream of interstate externalities and, in the MSA, divvied up the proceeds among the states.

If one thinks of the MSA payments as "damages" (their official, though, implausible, designation), the MSA amounts to a particularly rigorous application of the logic of modern products liability lawsuits. Under existing choice-of-law rules, defendant-manufacturers can be sued in a state and under a state's laws of the plaintiff's choice (usually, the plaintiff's home state). Since the manufacturers cannot control cross-border arbitrage (for example, by tailoring the price or design of a product to an individual state's liability regime and by preventing the import of "unsafe" versions of

---

285 *See supra* n. and sources cited *ibid*.

the product into a high-liability state), the costs of liability verdicts will be shared across the nation, while the benefits accrue entirely in-state. Each state has an incentive to expand liability.[286]

In a powerful article published a decade ago, Douglas Laycock argued that the choice-of-law doctrines that drive modern product liability litigation are unconstitutional.[287] A systematic preference for home-state law in interstate disputes, Laycock argued, violates the basic premise of equality among states and their citizens, which underpins the structure and logic of the Constitution and several of its specific clauses. One need not accept Laycock's dramatic conclusion to acknowledge that cross-border exploitation under the heading of "liability" is sufficiently problematic to trigger the Compact Clause. As noted *ad nauseam*, that Clause was meant to protect states against more than "sister"-state practices that are already unconstitutional under some other constitutional provision—for the excellent reason that such practices become more troublesome, not less so, when states exercise them collusively.

The MSA, moreover (and in any event), systematizes cross-border exploitation in several ways. First, it ensures that the costs are paid by consumers, rather than the defendant-corporations' workers and shareholders. Second, it provides that the proceeds go into the states' treasuries, rather than harmed individuals. In other words, while the MSA's price effects reduce future consumption, the MSA severs liability from the state purposes of deterrence and compensation that might otherwise be thought to justify an

---

286 Michael McConnell, *A Choice-of-Law Approach to Products-Liability Reform*, NEW DIRECTIONS IN LIABILITY LAW 90 (Walter Olson ed.)(1988).

287 Douglas Laycock, *Equal Citizens of Equal and Territorial States: The Constitutional Foundations of Choice of Law*, 92 COLUM. L. REV. 249 (1992).

incidental effect on interstate commerce. Third, the MSA imposes liability, or at any rate payment obligations, on producers who were not parties to the litigation nor, for that matter, even in existence at the time of its instigation or conclusion.

The payments retain some attributes of damages. But those are trivial; it is more natural to think of the "damages" as a tax.[288] If that thinking is correct, the payment obligations are an extraterritorial tax that would clearly be unconstitutional if any one state attempted to impose it. (An attempt by, say, Minnesota to impose a national excise tax would be obviously unconstitutional; the only question is whether the states, acting in concert, may bring about that feat.) Professor Ayres has identified "this extraterritorial due process challenge [as] the strongest grounds for attacking" the MSA and state settlements[289]—and identified its shortcomings: no competent plaintiff can be found. The case, moreover, would have to be litigated in front of a state court, and "we should not put great faith in state tribunals being able to make [a] disinterested determination of either th[e] standing question or the underlying substantive issue."[290] While that may be a slight overstatement,[291] Ayres is surely right on the larger, central point: supremacy alone is an uncertain business, and courts cannot be relied upon. That was James Madison's

---

288 Dagan & White, *Injurious Industries*, 75 N.Y.U. L. REV. at 426.

289 Ayres, *Tort Settlements*, 34 VAL. U. L. REV. at 603.

290 *Id.* at 603-04 (footnote omitted). An excellent reason for that suspicion, which Ayres does not fully spell out, is that a state court could invalidate only its own state's extraterritorial taxation. Other states' impositions on the state's citizens would remain unaffected.

291 One plaintiff has managed to maneuver an extraterritoriality claim against the MSA into federal court: *Star Scientific v. Beales*, 278 F.3d 339, 355-56 (4th Cir. 2002)(rejecting that claim). Star Scientific's claim differed differed from the theory sketched by Ayres in two respects: it was asserted under a dormant Commerce Clause (rather than Due Process) theory, and it concerned not the Settling Manufacturers' "damages" but the MSA provisions for Non-Participating Manufacturers' escrow payments.

case for the negative, and with respect to state compacts, the Convention emphatically agreed. The MSA and its fate in the court prove the Founders' wisdom.

Federal Interests. *Star Scientific*, to date the only appellate and, hence, the leading judicial decision on the MSA's compatibility with the Compact Clause, held that the agreement passes muster under the *U.S. Steel* precedent: the MSA does not encroach on federal power or interfere with federal supremacy, and it authorizes no state authority that the states could not exercise in its absence.[292]

The application of the *U.S. Steel* test to the MSA is not so straightforward as the court's cursory discussion suggests. For instance, if Ayres' extraterritorial taxation theory is plausible, then the MSA quite clearly exceeds every individual state's authority, and the question becomes whether the states may do by collusion what they may not do alone. *Star Scientific*, moreover, dispenses even with the *U.S. Steel* pretense that the test is one of *potential* impact on federal authority,[293] and instead looks exclusively to actual conflicts between the MSA's provisions and federal law. It finds such conflicts lacking on account of the MSA's savings clauses, which render the agreement enforceable only to the extent that it is consistent with now and future federal law (such as the Bankruptcy Code).[294] While it is certainly comforting to learn that the parties to the MSA did not intend to repeal the Supremacy Clause of the U.S. Constitution, the inclusion of savings

---

[292] *Star Scientific v. Beales*, 278 F.3d 339, 360 (4th Cir. 2002).

[293] *See supra* nn. and accompanying text.

[294] *Star Scientific v. Beales*, 278 F.3d at 360.

clauses indicates a belief on their part that the MSA might very well present conflicts with federal law.

Provisions of the MSA that were not before the *Star Scientific* court are equally problematic. For example, the MSA's advertising prohibitions and regulations appear quite clearly preempted by federal law.[295] The MSA's compatibility with federal antitrust law is a very close question.[296] And, in negotiating the financial terms of the MSA, the parties were—under the plaintiffs' own idiosyncratic theory—bargaining over the recovery of the federal government's money and its contractual claims under the federal Medicaid statute.[297] One could argue, on the authority of *U.S. Steel*, that the Compact Clause requires approval only for compacts that affect the federal government's

---

[295] Compare *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525 (2001) (holding that Massachusetts tobacco advertising regulations are preempted by Federal Cigarette Labeling and Advertising Act) with MSA III (stipulating content restrictions on tobacco advertising). Of course, tobacco manufacturers may voluntarily agree to advertising restrictions. The entry of such an agreement by a state court, however, is more than a mere notarization of a private contract, especially when the agreement purports to govern the rights and obligations of third parties (in the instance of the MSA, non-participating manufacturers). It is an official state act that is subject to ordinary preemption analysis. To be technical about it, that analysis affects only the entry of the MSA in the various states, not the MSA itself. But since the MSA requires entry by state court consent decree in every state, the practical effect is the same.

[296] *See* the careful, extended discussion in *Bedell v. Philip Morris*, 263 F.3d 239 (3rd Cir. 2001). The obvious federal antitrust implications of a tobacco deal were a principal reason for the submission of the Resolution for congressional approval. Bulow & Klemperer, *The Tobacco Deal* at 324. At the time, the Federal Trade Commission voiced grave reservations about the Resolution and its compatibility with federal antitrust law, and the proposed congressional legislation contained an explicit antitrust exemption. The equally problematic MSA itself has of course received no such dispensation.

[297] The federal government affirmatively asserted its claims on the payments, to the shrill protests of the state officials who were doing the negotiating. *See, e.g.*, John Schwartz, *States Want U.S. Out of Tobacco Deal*, WASH. POST Nov. 12, 1997, A-21. In May 1999, months after the enactment of the MSA, Congress explicitly disavowed its interest in the funds and authorized each state to use MSA proceeds "for any expenditures determined appropriate by the State." P.L. 106-31 (May 21, 1999), 113 Stat. 103 (amending Sec. 1903(d)(3) of the Social Security Act, 42 U.S.C. 1396b(d)(3)). Arguably, the federal Medicaid legislation constitutes an implied congressional consent to the MSA. *See Star Scientific v. Beales*, 278F.3d at 357-58 (summarizing defendants' argument to that effect). The court declined to address the argument, presumably because it found that the MSA did not require consent in any event. It is to my mind implausible, *see infra* nn. and accompanying text. In any event, the need to disavow the federal government's claims only confirms that those claims were in fact affected by the MSA.

supremacy, as distinct from its contractual rights vis-à-vis the states. Like so many tenets of Compact Clause doctrine, however, that claim cannot possibly be right.

Star Scientific reflects the poverty of modern Compact Clause analysis: it reduces the judicial inquiry to a search for an enhancement of the power of the states, collectively, "quoad the national government" (in the *U.S. Steel* Court's weird phraseology). It then finds such an enhancement only in the event of an actual conflict with federal law, thus rendering the Compact Clause wholly academic. (The true holding of *Star Scientific* is that the Clause is unenforceable.) The step from potential impact to actual conflicts is, for amply noted reasons, a clear error. The larger, more fateful error lies in the first step—that is, in the demise of federalism's horizontal, state-to-state dimension and the purpose, central to the Compact Clause, of preventing states from ganging up on sister-states. The MSA illustrates the dangers that attend the evisceration of that protection: a handful of states set in motion a process that drove all states, many of them unwilling and some bitterly opposed, into a uniform regulatory and tax scheme.

The MSA amounts to the spontaneous, extra-constitutional and extra-congressional creation of a federal grant-in-aid system: the proceeds of national tax on tobacco consumption are transferred to states that agree to abide by certain restrictions.[298] Such programs are the stock-in-trade of the American welfare state, but they are not entirely unproblematic. While states are nominally free to participate or not in a given

[298] While the comparison may seem far-fetched at first sight, it naturally occurred to one of the nation's most knowledgeable and renowned students of federal-state relations. The final negotiation of the MSA, Martha Derthick has written, "was as if the [negotiating] group had been constituted to perform legislative acts […] [L]itigants and tort lawyers would now sit down, much as Congress does when it legislates grants-in-aid, to distribute benefits among the states." DERTHICK, UP IN SMOKE 171.

program, the fact that each state's citizens will pay a share of the program costs even if their state declines to accept the benefits renders an autonomous choice illusory. In the absence of a credible constitutional commitment against interstate redistribution, the states' pre-enactment strategy is strongly biased in favor of legislation—lest the states that favor intervention in any event massage the distribution formula further to their advantage. *Post*-enactment, the states' default strategy is to change the mix of federal funds and obligations in their favor. Barring truly exceptional circumstances, defection becomes impossible even if the federal grant pays only a fraction of the program cost (the usual case), and even if the state pays a disproportionate share (relative to sister-states) of the program cost.[299]

While the asymmetry of costs and benefits that drives grants-in-aid and conditional funding statutes may not constitute "coercion" in a constitutionally significant sense,[300] some scholars have come to view those dynamics as so corrosive of constitutional federalism norms, and so conducive to horizontal exploitation, as to

---

[299] Edward A. Zelinsky, *Unfunded Mandates, Hidden Taxation, and the Tenth Amendment: On Public Choice, Public Interest, and Public Services*, 46 VAND. L. REV. 1355 (1993); Michael S. Greve, *Against Cooperative Federalism*, 70 MISS. L. J. 557, 594-98 (2000). The empirical evidence overwhelmingly supports this analysis: one cannot readily think of a single case in which even a few states, let alone a majority of states, have advocated the abolition of a burdensome federal grants program.

[300] That, of course, is the generally accepted view of the matter. In *Massachusetts v. Mellon; Frothingham v. Mellon*, 262 U.S. 447 (1923), the Commonwealth of Massachusetts and individual Massachusetts taxpayers challenged the federal Maternity Act, which extended federal funding to states that agreed to participate in a federal entitlement program. Massachusetts argued that the statute effectively coerced the state into participating, since her citizens would be asked to pay a share of the federal tax revenue in any event. The Supreme Court dismissed the state's and the taxpayers' cases on jurisdictional grounds. (For a trenchant analysis of this aspect of the decision and its nexus with the merits *see* Richard A. Epstein, *Standing and Spending—The Role of Legal* and *Equitable Principles*, 4 CHAPMAN L. REV. 1 (2001)). Having done so, the Court added that the state could avoid the "coercive" effects of the federal statute "by the simple expedient of not yielding." *Massachusetts v. Mellon*, 262 U.S. at 482. The Supreme Court has left open the possibility that some federal funding statutes may be unconstitutionally coercive: *South Dakota v. Dole*, 483 U.S. 203 (1987). The "coercion," however, lies in the disadvantageous mix of federal funding and state obligations and in the lack of a nexus between the two, not in the asymmetry between taxpayer burdens and receipts.

warrant judicially enforced controls.[301] While theirs is (still) a minority view, it is sufficiently powerful to merit a response. That response must rest on the ground that grants-in-aid schemes are legislated in and by the United States Congress, where states can mobilize and exercise opposition, and where a multitude of competing interests may help to thwart excessively partial legislation, *before* those schemes unfold their inescapable economic dynamics. Federalism's process protections constitute the bare constitutional minimum.

The process that produced the MSA mirrors the dynamics of grants-in-aid legislation—with one crucial difference. The Resolution (the MSA's precursor) collapsed in Congress under the weight of interest group conflicts. In other words, it failed for the constitutionally envisioned reason. And so the MSA's architects moved to a less open and cumbersome process of negotiation, where the range of interests could be restricted and the hold-out states were left without a realistic chance.[302] The congressional consent requirement of the Compact Clause would provide a safeguard against that maneuver. In

---

301 S*ee, e.g.*, Ilya Somin, *Closing the Pandora's Box of Federalism: The Case for Judicial Restriction of Federal Subsidies to State Governments*, ___ GEO. L. REV. ___ (2001) (arguing that virtually all federal grants programs to states are unconstitutional under *New York v. United States*, 505 U.S. 144 (1992)); Joshua D. Sarnoff, *Cooperative Federalism, the Delegation of Federal Power, and the Constitution*, 39 ARIZ. L. REV. 205 (1997) (arguing that general revenue sharing constitutes excessive delegation of legislative power); and especially Lynn A. Baker, *The Spending Power and the Federalist Revival*, 4 CHAPMAN L. REV. 195, 219-220 (2001): "While [process federalism] may well ensure that '*state interests as such*' are protected against federal oppression, *federal* oppression is not the problem. The problem, rather, lies in the ability of *some states* to harness the federal lawmaking power to oppress *other states*." (emph. in the original; footnotes omitted). Baker's contention that such oppression will occur with great regularity is buttressed by public choice theories that predict, on the basis of a very modest assumption of information asymmetries between state officials and their citizens, that the adoption of a redistributive program in some states will eventually produce a federal mandate, by virtue of dynamics paralleling those that produced the MSA. Supermajoritarian obstacles at the federal level may not suffice to counteract that tendency. Edward A. Zelinsky, *Unfunded Mandates, Hidden Taxation, and the Tenth Amendment: On Public Choice, Public Interest, and Public Services*, 46 VAND. L. REV. 1355 (1993).

302 David S. Samford, *Cutting Deals in Smoke-Filled Free Rooms: A Case Study in Public Choice Analysis*, 87 KY. L. J. 845, 886-92, 899-900 (1999) (broader range of interests prevented approval of the Resolution in Congress; exclusion of many interests, including public health advocates, facilitated state-based settlement process).

dismantling that safeguard, the judiciary has dismantled an enforceable constitutional protection for federalism. The courts' position smacks in that regard of a process federalism that recognizes no judicially enforceable federalism norms.[303] But that characterization is unfair to process federalism: extant Compact Clause theory, assuming it deserves that honorific, will not even protect the process.[304]

VII. Toward a Constitutional Compact Clause Doctrine

A. James Madison, Functionalist?

The Compact Clause, I have argued, is the Madisonian negative in a specified range of application. Its purpose is to invert the ordinary, "mere supremacy" rule operating on state enactments. One can argue with perfect justice that courts ought to respect and enforce the constitutional arrangement—and leave it at that. The structural argument for the Compact Clause can stand on its own, without the crutch of a functional analysis. The purpose and, as it were, the function of that analysis is simply to explicate the background presumption of the Compact Clause. Just as the United States

---

[303] *See* Herbert Wechsler, *The Political Safeguards of Federalism: The Role of the States in the Composition and Selection of the National Government*, 54 COLUM. L. REV. 543 (1954). The most forceful articulation of a neo-Wechslerian perspective is Jesse Choper, JUDICIAL REVIEW AND THE NATIONAL POLITICAL PROCESS (1980). For one of the many critiques of the Supreme Court's "somewhat stunning" reliance on Wechsler and Choper—prior to its recent re-discovery of federalism—*see* Barry Friedman, *Valuing Federalism*, 82 MINN. L. REV. 317, 325 (1997) (citing and briefly discussing those critiques). For a rare but valiant neo-neo-Wechslerian defense of process federalism as something different from rank nationalism see Larry Kramer, *Understanding Federalism*, 47 VAND. L. REV. 1485 (1994); and Kramer, *Putting the Politics Back Into the Political Safeguards of Federalism*, 100 COLUM. L. REV. 215 (2000).

[304] In this context, it is worth noting that even *Garcia v. Metropolitan Transit Authority*, 469 U.S. 528 (1985), the high-water mark of the Supreme Court's process federalism, contemplated judicial protections of the political process itself. *See Garcia*, 528 U.S. at 554 (judicially enforced federalism norms should be "tailored to compensate for possible failings in the national political process.")

Constitution makes sense only against a background presumption in favor of private orderings (why else encumber political institutions with checks and balances?), so the Compact Clause makes sense only against a background presumption against state agreements—more precisely, a presumption that such agreements, as a class, are problematic in a way in which run-of-the-mill enactments by an individual state are not. The transaction cost analysis shows that presumption to be warranted, and the compact risks it delineates parallel the Founders' apprehensions.

No: James Madison did not anticipate the *specific* dangers and arrangements just discussed. Conversely, he and his contemporaries had every reason to contemplate dramatic compact risks that no longer concern us, including the fear that economic warfare among the states might well engender actual war and the complete destruction of the Union. To deny these manifest differences is to invite ridicule. One easily dismissed complaint against the MSA characterized the agreement as a "tax confederacy on American soil."[305] The phrase, and the fear it conjures up, seem grossly overwrought.

And yet, the image of a single-purpose confederacy captures, albeit awkwardly, the common theme of Madison's nightmares and modern-day compacts—the problem of factionalism in a federal republic. Factionalism was the central theme of Madison's campaign for a congressional negative. Factionalism, too, is the theme behind regulatory compacts. The dangers posed by regulatory compacts—compact formation at the behest of local interests seeking to thwart federal intervention; the deliberate infliction of externalities; cartelization and exploitation; the evasion of accountability and responsibility—are so many facets of interest group bargains and political

[305] *Hise v. Philip Morris, Inc*., 46 F.Supp.2d 1201, 1210 (N.D. Ok. 1999) (citing plaintiffs' complaint).

accommodation. (Empirical studies show that regulatory compacts are typically a response to interest group demands at the state level.)[306] None of this would have struck Madison as far-fetched or unexpected.

Madison proposed a comprehensive negative as an essential safeguard against faction. The Convention rejected that proposal and instead limited the negative to state actions that could be expected to have substantial detrimental effects on sister-states and their citizens—including, of course, state compacts. Madison himself viewed this attempt to arrest factionalism at the borders as inadequate. But the Convention's strategic choice reflects his intuitions to the extent that state factionalism is both more likely and more dangerous when it crosses borders—more likely, because schemes that impose costs on outsiders only face little internal opposition; more dangerous, because cross-border exploitation undermines the foundations of constitutional federalism.[307]

Federalism must start with a premise of formal equality among states—not because they are in fact equal, but because no other genuinely federal principle is plausible.[308] This in turn implies a principle of non-aggression and non-discrimination

---

306 *See, e.g.*, BARTON, INTERSTATE COMPACTS 8-33 , 164; WILLIAM E. LEUCHTENBURG, FLOOD CONTROL POLITICS:THE CONNECTICUT RIVER VALLEY PROBLEM, 1927-1950, 250 (1953); and PARRIS N. GLENDENING & MAVIS MANN REEVES, PRAGMATIC FEDERALISM 199 (1977).

307 The edifice need not tumble; we can prop it up in all sorts of ways. But it is then no longer the same building.

308 Some "federal" systems (such as Germany) have departed from formal equality and have instead constitutionalized principles principles of *material* equivalence and solidarity among states. Such systems, however, entrust the central authority with an affirmative obligation to redress inequalities that might newly emerge from, among other things, the exercise of state autonomy. Unlike our federalism, this brand of federalism reduces the states' "autonomy" to the independent administration of federal programs. For a sophisticated defense of administrative federalism and a proposal to establish it on American soil see Roderick M. Hills, Jr., *The Political Economy of Cooperative Federalism: Why State Autonomy Makes Sense and 'Dual Sovereignty' Doesn't*, 96 MICH. L. REV. 813 (1998). For a rather more skeptical perspective see Michael S. Greve, *Against Cooperative Federalism*, 70 MISS. L. J. 557 (2000).

among states: in a world of equal (contiguous) states, limited territory, and scarce resources, no other principle makes sense. In protecting against unapproved state agreements to the detriment of sister-states, the Compact Clause reflects both these principles. The inversion of the default rule—relative to the mere supremacy rule that operates on single-state enactments—is, admittedly and especially by Madisonian lights, an imperfect arrangement, since states may easily pursue factional schemes to the detriment of sister-states even when they act alone. We have in recognition of that reality created a broader negative and called it the dormant Commerce Clause. As a constitutional first cut, however, the Compact Clause rule is perfectly reasonable. It guards against the distinct risks of collusion and, in so doing, ensures a rough equality and reciprocity.[309]

The twin presumptions of equality and non-aggression in place, federalism must organize the exchanges that states may wish to undertake. Some exchanges, called treaties, threaten such a dramatic departure from the initial, equal allocation of entitlements that the Constitution subjects them to a *per se* prohibition. That rule, though, when applied to all state bargains, would suppress beneficial agreements along with nefarious ones. The constitutional task, then, is to allow mutually beneficial bargains, while guarding against the constitutional risk. To that end, the Compact Clause provides a monopolistic forum and procedure for all other exchanges. In that forum, under those procedures, states may cooperate. They may even change the original allocation of entitlements and collude to exploit sister-states. But they must do so within the constitutional bounds and through the established, agreed-upon procedures and

[309] The fact that additional safeguards may be necessary certainly provides no reason to underenforce the existing ones. *See infra* nn. and accompanying text.

institutions. A principle that would allow everyone to defect from that arrangement would satisfy the demand of equality; but it is a lottery for the states, not a principle on which they can rely. Therefore, equality requires the categorical rule of the Compact Clause: no one may defect.

By emasculating the congressional approval requirement, and by reducing Compact Clause analysis to its vertical, federal-state relation, the Supreme Court's Compact Clause invites defection—in the name of, of all things, "harmony" and "federalism."[310] The functional analysis just presented, in contrast, emphasizes federalism's horizontal dimension—the question of what equal states may and may not do to each other. Extant doctrine views federalism as a kind of shorthand for the states' opportunistic agenda; the functional analysis insists that federalism must respect the states' equality and integrity. In so insisting, it tracks the logic of the Compact Clause and the larger federal architecture.

The functional analysis is consistent with the conclusion that the Compact Clause ought to be enforced as written. But it does not quite compel that conclusion. The identification of four discrete (though connected and overlapping) compact risks may allow a more nuanced and perhaps efficient Compact Clause rule than the Founders' congressional approval requirement for any and all state agreements. Unlike the Compact Clause, the functional analysis contemplates the existence of a set of exchanges that can, *ex ante*, be shown to pose no constitutional risk, and which should therefore be exempt from the negative.

---

[310] *See, e.g., New York v. O'Neill*, 359 U.S. 1, 6 (1959) (quoted *supra* in the text accompanying n. 28).

While this approach will turn out to have its own problems,[311] it is worth exploring for pragmatic reasons. The full-blown Madisonian argument runs up against adverse Supreme Court precedent, cooperative enthusiasms, and entrenched interests. The perceived overbreadth problem of the Compact Clause has provided the impulse, as well as a patina of plausibility, for the emasculation of the Clause; insofar as a functional interpretation addresses that concern, it may aid in reviving the Clause. The Madisonian argument, moreover, bumps up against a federalism that begins and ends with the protection of "the states," collectively, against the national government. To the distressing extent that the modern Supreme Court's rediscovery of federalism rests on federalism's "etiquette" and the "sovereignty" and "dignity" of states as political entities, it may impede a rediscovery of the Compact Clause.[312] That consideration, too, counsels a search for a manageable doctrine that sweeps no more broadly than is absolutely necessary to enforce the core purposes of the Compact Clause.

To be sure, the conciliation can only go so far. Any Compact Clause doctrine that is remotely faithful to the constitutional text and structure, for example, will conclude that *U.S. Steel* was preposterous in its reasoning and wrong in its outcome. Any such

---

311 *See infra* nn. and accompanying text.

312 The Supreme Court's preoccupation with federalism's expressive dimension has attracted severe (and to my mind deserved) criticism. *See, e.g.*, Evan H.Caminker, *Judicial Solicitude for State Dignity*, 574 ANNALS OF THE AMERICAN ACAD. OF POL. & SOC. SCI. 81 (Mar. 2001). The distance between a dignity- and sovereignty-centered federalism and the real Madisonian thing is nicely illustrated by Madison's angry challenge:

> Was … the American Revolution effected, was the American Confederacy formed, was the precious blood of thousands spilt, and the hard-earned substance of millions lavished, not that the people of America should enjoy peace, liberty, and safety, but that the governments of the individual states, that particular municipal establishments, might enjoy a certain extent of power and be arrayed with certain dignities and attributes of sovereignty?

FEDERALIST PAPERS No. 45 (Madison), 289.

doctrine likewise compels the conclusion that the MSA is unconstitutional. Still, it can be shown that a functional Compact Clause doctrine that is faithful to the constitutional structure can incorporate and explain many and perhaps most Compact Clause precedents. Moreover, such a doctrine is broadly consistent with, and may in fact reinforce, the two most attractive features of the modern Supreme Court's federalism—the partial revival of enumerated powers, and the emphasis on political accountability. [313]

B. A Functional, Constitutional Compact Clause Test

The Test. I follow extant Compact Clause doctrine in assuming that a state agreement or compact, in the constitutionally relevant sense, must impose an enforceable contractual obligation, for the duration of the arrangement, on the participating states.[314] I assume, moreover, that an agreement or compact in the constitutionally relevant sense requires participating states to act in their official capacity *as states*, not in a proprietary or market-participant capacity.[315] Once such a state agreement has been shown to exist without congressional approval, a constitutional challenge for lack of congressional consent should succeed if the plaintiff makes a credible showing that the compact, reasonably construed, poses one of the four now-familiar risks—an exercise of powers concurrently possessed by the Congress; interstate externalities; cartelization; or agency problems, including a dilution of political accountability and a delegation of state legislative or executive power. Defendants may rebut that case by proving that the

[313] I have argued elsewhere that enumerated powers and anti-delegation arguments—rather than "states' rights" protections under the Tenth and Eleventh Amendment—constitute the most attractive features of the Supreme Court's federalism. MICHAEL S. GREVE, REAL FEDERALISM 79-82 *et pass*.

proposed compact poses none of those risks. Absent such a showing, the compact is void without congressional consent.

In requiring plaintiffs to establish no more than a reasonable likelihood—while requiring defendants to prove that no such likelihood exists—the proposed test stacks the deck in favor of the plaintiff. That is intentional, and necessary to afford the Compact Clause any room at all. Even the *U.S. Steel* Court purported to hold that the test under the Compact Clause is one of *potential* rather than real effects.[316] The Court proceeded, however, to ignore that pronouncement and effectively required the plaintiffs to prove that the MTC infringed on federal supremacy. Shifting the burden of proof in Compact Clause cases to defendants is a procedural means of re-orienting the judicial inquiry towards risks and potentialities, rather than certainties.

Precedents and Conceptual Lines. The Supreme Court has tended to scrutinize the effects of individual compacts on a case-by-case basis.[317] The proposed test, in contrast, turns on compact risks *per se*, rather than on the expected effects of any

---

314 *E.g, Northeast Bancorp v. Bd. Of Governors of Fed. Reserve*, 472 U.S. 159, 175 (1985).

315 State A's purchase of electric power from publicly owned utility in state B is an ordinary contract, not an agreement or compact requiring congressional consent. Similarly, and notwithstanding hysterical assertions that enforcement of the Compact Clause might lay waste to the National Association of Governors or the National Association of Attorneys General (NAAG) (*see, e.g.*, Ferguson, supra n.), *ex officio* lobbying and information-sharing associations of state officials are not agreements or compacts among states *as states*. Where such organizations play a role in negotiating, administering, and enforcing an agreement or compact, it is that instrument, not the sponsoring organization, that requires congressional approval. Likewise, the NAAG's enforcement guidelines and increasingly common multistate enforcement actions, especially for alleged antitrust and consumer protection violations, present a variety of political, economic, and legal problems. Barring an enforceable mutual obligation, however, they do not present a Compact Clause problem. Note (Jason Lynch), *Federalism, Separation of Powers, and the Role of State Attorneys General in Multistate Litigation*, 101 COLUM. L. REV. 1998, 2016-22 (2001).

316 *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 472 (1978).

317 Engdahl, *Interstate Arrangements*, 64 MICH. L. REV. at 68.

individual compact, and in this manner substitutes a conceptual rule of decision for a case-by-case inquiry. If a particular compact is shown to be a cartel, it requires congressional consent; the magnitude of the effects is irrelevant. Likewise, a compact commission cannot be a little bit pregnant with delegated state powers; if it exercises such powers to any extent, the compact requires congressional consent.

A conceptual rule is appropriate to the structure of the Compact Clause, which commits an assessment of effects and consequences to the Congress rather than the courts. And in fact, despite the ad-hoc nature of the leading Compact Clause precedents, many of those precedents also imply, even though they do not articulate, sensible conceptual distinctions akin to the ones proposed here. Boundary compacts are one example; reciprocity agreements are another.

Binding Compact Clause precedents hold that a state agreement to demarcate more precisely a pre-existing boundary line does not require congressional consent.[318] A boundary *change*, in contrast, does require approval. That rule effectively imposes a conceptual distinction, rather than a raw case-by-case effects test; after all, one can easily imagine a (small, inconsequential) boundary change that would neither affect the supremacy of the United States nor entail adverse consequences for sister states. But it is *likely* that a boundary-changing agreement might have such consequences, and nothing more need be shown to bring the agreement under the ambit of the Compact Clause. The defendant state (or states), in contrast, must prove that those risks are non-existent, and the only way to do so is to show that the agreement does not in fact change a boundary.

---

[318] *New Hampshire v. Maine*, 426 U.S. 363, 369-70 (1976); *Virginia v. Tennessee*, 148 U.S. 503 (1893).

An analogous analysis applies to the judicial exemption of so-called reciprocity agreements from the Compact Clause and the congressional negative.[319] The functional test supplies a plausible rationale for this distinction: reciprocity agreements pose no danger of cartelization or third-party externalities, and they delegate no powers to another state or interstate agency.[320] Reciprocity agreements may affect areas where Congress is competent to legislate—foremost, interstate commerce. But they cannot burden that commerce and, in that fashion, interfere with federal prerogatives.

By way of illustration, varying and conflicting state regulations require nurses to obtain a license in the state where they wish to practice. Licensed nurses in each state attempt to restrict market entry by nurses licensed in another state,[321] thus creating a regulatory race to the bottom that requires some coordinated response. A state attempt to "solve" the coordination problem by means of regulatory harmonization, to be accomplished by an Interstate Nurse Licensing Commission, would pose dangers of cartelization, regulation in restraint of interstate commerce, and a delegation of state

---

[319] *Bode v. Barrett*, 344 U.S. 583 (1953); *Massachusetts v. Missouri*, 308 U.S. 1 (1939); *S.F.R. v. James*, 161 U.S. 545 (1896).

[320] A possible exception to this general proposition—and a difficult problem—is posed by reciprocity agreements that are by their terms limited to selected states. Such agreements might provide at least a piecemeal solution to state parochialism and interstate coordination problems, and a categorical, all-or-nothing non-discrimination rule might deter such advances. Still, the discriminatory and exploitative potential of selective agreements to my mind precludes an exemption from the congressional approval requirement.

As noted *supra* n. , the Supreme Court confronted the problem of selective reciprocity in *Northeast Bancorp v. Bd. Of Governors of Fed. Reserve System*, 472 U.S. 159 (1985). The most plausible defense of the state statutes there at issue—though not the Supreme Court's defense—is that the Douglas Amendment, as interpreted by the Federal Reserve Board, constituted an implicit congressional approval of selective state reciprocity agreements. That reading is admittedly problematic, but no more so (to my mind) than the Court's explicit holding, *id.* at 174, that the Amendment immunized the state laws against a dormant Commerce Clause attack. If that understanding of the Douglas Amendment is untenable, *Northeast Bancorp* was wrongly decided as to the Compact Clause claim.

[321] *See* Alex Maurizi, *Occupational Licensing and the Public Interest*, 82 J. POL. ECON. 299, 313 and sources cited *id.* (1974).

authority to a supra-state entity. Even if the arrangement could be shown to constitute a plausible response to an acute coordination problem, it should require congressional consent. In contrast, if states solved the problem through reciprocal recognition—such that each participating state recognizes the nursing licenses issued by another state—no risk of cartelization, externalities, or delegation arises. And while mutual recognition affects interstate commerce, it solves the coordination problem through private arbitrage rather than political harmonization—thereby liberating, not burdening, interstate commerce. In short, reciprocity or mutual recognition arrangements pose none of the identified risks, and may therefore be exempted from the Compact Clause negative.[322]

The fact that such disparate arrangements as boundary demarcations and reciprocity agreements should be found under the same, no-approval-required umbrella is explained by a thoroughly Madisonian argument. The dangers of compacts arise from the operation of faction. One-shot boundary demarcations do not implicate factions. Reciprocity agreements expose domestic factions to the winds of foreign competition. They signal that such factions have been crushed. The rare instances in which states manage to do so by agreement do not warrant the suspicion that attends to institutionalized interest-group bargains. We should instead greet them with a warm welcome.

Federalism and Compacts (I): Enumerated Powers. The perception that the textual Compact Clause is hopelessly overbroad has been a mainstay of Compact Clause

---

[322] I have found one explicit judicial articulation of this rationale: *General Express Ways, Inc. v. Iowa Reciprocity Bd*., 163 N.W. 2nd 413, 420 (Iowa 1968) ("[T]his being a purely fiscal arrangement *which was intended to encourage rather than restrain commerce among the states*, it is not the type of interstate contract which requires Congressional consent.") (emphasis added).

analysis since *Virginia v. Tennessee*. The functional Compact Clause test contemplates not only (as just noted) an exemption for boundary demarcations and reciprocity agreements but also, and for identical reasons, a "police power exemption."

The risk of state bargaining with rights that are held, solely or concurrently, by the national government does not obtain in areas where the national government has no rights—that is, beyond the purview of the enumerated powers and the Supremacy Clause. Hence, states need not necessarily obtain congressional approval for compacts that fall outside the scope of federal enumerated powers.[323] Such a limitation is obviously not part of the actual Compact Clause. But it may help to address the overbreadth concern, and it has the added advantage of dovetailing with both the precedents and the contemporary Supreme Court's federalism.

As suggested earlier, an implied "police power exception" to the Compact Clause was quite probably what Justice Field had in mind in penning his *dicta* in *Virginia v. Tennessee.*[324] The point was lost due to Field's lack of clarity, the cooperative enthusiasms of later generations, and the *de facto* renunciation of the enumerated powers doctrine. Arguably, the latter development contributed to the wholesale inversion of the Compact Clause in *U.S. Steel*. Recall Justice Powell's rejoinder to the dissenters' observation that the MTC presented a grave interference with federal supremacy: the

---

[323] If the compact violates other constraints (*e.g.*, by exposing sister states to externalities), it will still require approval.

[324] *Supra* nn. and accompanying text. One can find stray suggestions to the same effect in later cases. *See, e.g., New York v. O'Neill*, 359 U.S. 1, 11 (1959): "The Constitution of the United States does not preclude resourcefulness of relationships between states on matters *as to which there is no grant of power to Congress*." (emphasis supplied). *New York*, however, is an extended exercise in adjudication by free association, and the quoted passage no more constitutes a holding than anything else in the opinion.

dissent, Powell averred, confused federal interests with federal supremacy.[325] At the time of *U.S. Steel*, virtually nothing fell beyond the reach of congressional power (with the lone and soon-repealed exception of government employment conditions in areas of "traditional" state activity).[326] The Compact Clause would thus require congressional consent in literally all cases. Confronted with that conclusion, Powell limited the scope of the Clause in the only way he knew: instead of requiring consent for all compacts that *fall under the umbrella* of federal supremacy (and thus "interest" the federal government), he restricted it to compacts that actually *conflict with* it. For reasons discussed at great length, that conclusion is very wrong.

The Supreme Court's partial rediscovery of the enumerated powers doctrine over the past decade provides an opening for a supremacy exemption that is broadly consistent with the Compact Clause or at least, does not turn it on its head. Under a functional test (though not, to repeat, under the original Compact Clause), states would need no congressional consent to form a compact on the prevention of gender-based violence, which we know to be beyond the jurisdiction of the United States Congress.[327] I also assume, although we do not yet know, that states are free to negotiate and enforce an interstate compact on the prosecution of purely in-state and non-economic crimes, such as the possession of drugs.[328] A state agreement regulating isolated wetlands (for

---

325 *U.S. Steel Corp. v. MTC*, 434 U.S. 452, 479 and *id*. n. 33 (1978).

326 *National League of Cities v. Usery*, 426 U.S. 833 (1976); overruled in *Garcia v. Metropolitan Transit Authority*, 469 U.S. 528 (1985).

327 *United States v. Morrison*, 529 U.S. 598 (2000).

328 I assume that a federal provision of this type would fall outside the scope of the Commerce Clause as interpreted in *United States v. Lopez*, 514 U.S. 549 (1995) and *United States v. Morrison* , 529 U.S. 598 (2000). Lower courts have split on the question. *See* Brannon P. Denning & Glenn H. Reynolds*, Rulings*

instance, to facilitate cross-border swaps for mitigation purposes) may likewise be permissible without congressional approval.[329] The scope of compacts that require no congressional approval expands as the scope of enumerated powers contracts. If the federal government lacks the power to legislate on the interstate enforcement of child support obligations, state compacts to that end require no congressional approval. If Congress does possess that authority (as appellate courts have held), such compacts require approval.[330]

More controversially, the functional analysis suggests that state compacts that affect federal spending do not, by virtue of that fact alone, require congressional consent. A number of interstate arrangements, such as various education compacts to which many states are parties, regulate and coordinate state functions that are typically performed under federal spending statutes. These compacts are of obvious "interest" to the national government in the sense that they might affect the distribution of federal funds. (The appropriation of funds itself evidences a federal interest.) Federal spending, though, is not an "interest" of the sort that should trigger the congressional consent requirement, because the exercise of the spending power is not an exercise of federal supremacy in the same way in which, say, a regulation of interstate commerce is an assertion of federal

---

and Resistance: The New Commerce Clause Jurisprudence Encounters the Lower Courts (law review mscr. On file with author) (surveying post-*Morrison* case law).

329 *See Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159 (2000) (suggesting, but not holding, that regulation of wetlands isolated from waters of the United States exceeds scope of congressional authority under the Commerce Clause).

330 All appellate courts that have addressed the question have held that the federal Child Support Recovery Act, **stat cite**, constitutes valid Commerce Clause regulation. *See, e.g., United States v. Faasse,* 265 F.3d 475 (6th Cir. 2001)(en banc). But *see id.* at 494 (Batchelder, J., diss.) (arguing that the statute does not regulate interstate commerce and therefore exceeds congressional authority). **[add state compacts**]

supremacy.[331] States must of course comply with the contractual obligations they have agreed to undertake in exchange for federal funding, but they cannot "interfere" with federal spending in the way in which they may—and often do—interfere with federal regulation under an enumerated power. Suppose the states agreed, one and all, to refuse federal funding for sexual abstinence education:[332] While that agreement would obviously frustrate federal objectives, it cannot be said to interfere with national supremacy. The states simply agree to restrict, by mutual agreement, their otherwise unlimited autonomy to accept or reject federal funds. They are bargaining with and over rights that belong to them exclusively, and no congressional approval may be required.[333]

Compacts and Federalism (II): Agency and Delegation. Under a functional Compact Clause test, a credible showing that a compact poses a risk of delegating state power and of diluting the political accountability of state officials would trigger the congressional consent requirement. By that standard, state agreements that establish standing interstate commissions and administrative bodies should be subject to a *per se*

---

331 A federal Spending Clause statute trumps, supersedes, or preempts nothing. Its force stems entirely from the state's acceptance of the funds; if a state refuses to accept the money, nothing follows. For a forceful scholarly presentation of this view *see* David Engdahl, *The Spending Clause*, 44 DUKE L. REV. 1 (1994). For an explicit judicial endorsement *see Westside Mothers v. Haveman*, 133 F.Supp.2d 549 (E.D.Mich. 2001) (*appeal pending*) (federal eligibility requirements under Medicaid statute do not constitute exercise of federal supremacy). The same perspective is implied by the U.S. Supreme Court's characterization of Spending Clause statutes as being "in the nature of a contract." *Pennhurst State Sch. & Hosp. v. Halderman*, 451 U.S. 1, 17 (1981).

332 The federal program, 42 U.S.C. 710, is one of the exceedingly rare federal funding programs for which states have refused to accept funding. See Lynn Smith, *Chastity Makes a Comeback*, L.A. TIMES Aug. 10, 1999, A-1 (describing California's refusal to accept funding).

333 The proposition requires important provisos. The argument assumes, first, that Congress lacks the authority to regulate the funded state activities directly, under its enumerated powers. (With respect to education, that assumption may be inferred, though with no great confidence, from *United States v. Lopez*, 514 U.S. 549 (1995)). It assumes, second, that the state compact in question does not purport to violate or circumvent federal strictures with which the compacting states have agreed to comply as a condition of

requirement of congressional approval, at least to the extent that such agencies perform more than merely consultative or information-gathering functions:[334] any such body might wind up exercising delegated state powers, and that risk alone suffices to trigger the Compact Clause negative.[335] The special suspicion of compact commissions is broadly consistent with extant precedent,[336] and it dovetails with the Supreme Court's federalism decisions. In fact, read for all they are worth, those decision very nearly compel the *per se* rule.

In the course of its partial rehabilitation of the enumerated powers doctrine, the Court has also resurrected the principle that the states may not delegate their sovereign (police) powers to the Congress. That injunction is inherent in the notion of limited, enumerated powers.[337] Nothing follows from it, practically speaking, if congressional

---

receiving federal funds. Finally, the argument assumes that the state compact at issue does not threaten other, independent federal interests. *See infra* nn. and accompanying text.

[334] An exception for information-gathering functions finds some support in Supreme Court's federalism jurisprudence: in *Printz v. United States*, 521 U.S. 898, 917-18 (1997), the Supreme Court suggested that a constitutional prohibition against the federal "commandeering" of state officials does not extend to federal mandates requiring state data collection and maintenance. The most plausible rationale for this exception is that data collection is merely a ministerial rather than a true sovereign state function. Analogously, a delegation of such functions to a state compact commission seems less troublesome than a delegation of sovereign, coercive powers.

[335] Since state cartels almost invariably require joint administration, *see supra* nn. and accompanying text, a *per se* rule that subjects such instruments to congressional approval also buys protection against state cartels. That may be a considerable advantage, since the anti-joint-body rule is bound to be subject to fewer judicial errors than an anti-cartel rule.

[336] *See Northeast Bancorp v. Bd. Of Gov. of the Fed. Reserve Sys*., 472 U.S. 159, 175 (1985) (joint body "indicia" of compact); *Star Scientific, Inc. v. Beales*, 278 F.3d 339, 360 (4th Cir. 2002) (administrative body created by MSA establishes compact).

[337] The anti-delegation principle was stated explicitly in several cases decided in (dual) federalism's heyday. *See, e.g*., *In re Rahrer,* 140 U.S. 545, 560 (1891) (citing *Gunn v. Barry*, 82 U.S. (15 Wall.) 610, 623 (1872*); United States v. Dewitt*, 76 U.S. (9 Wall.) 41, 45 (1869); and *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299, 304 (1851)). Contemporary cases acknowledge the principle by implication. We know, for example, that the endorsement of a federal civil remedy for gender-based violence by a large majority of states does not render such regulation constitutional. *United States v. Morrison*, 529 U.S. 598, 653 (2000) (Souter, J., diss.) (noting states' *amicus* support for federal enactment). The majority opinion in

powers are not actually enumerated (or, what amounts to the same thing, enumerated but unlimited). But while that was pretty much the Supreme Court's federalism riff at the time of *U.S. Steel*, subsequent decisions—in particular and most explicitly, the 1992 decision in *New York v. United States*[338]—have partially restored federalism's logic.

New York invalidated a core provision of the 1985 Low-Level Radioactive Waste Policy Amendments Act.[339] Intriguingly, though of no direct consequence to the delegation point here at issue, the Act represented a congressional attempt to encourage the formation of state compacts for the disposal and storage of low-level nuclear waste. The convoluted statutory scheme established by the Act essentially subjected states that failed, within a certain timeframe, to join a congressionally approved compact to a severe federal regulatory regime, obligating each state to provide for the disposal of waste created within their borders. That approach had been developed and urged upon Congress by the states, acting under the umbrella of the National Governors Association (NGA).[340] In 1990, New York, one of the few states that had failed to join a regional compact, challenged the statute on Tenth Amendment and other grounds. While sustaining large portions of the statutory scheme, the Supreme Court found that a so-called "Take Title" provision—one of the statutory "incentives" to pressure states into implementing, by compact or on their own, acceptable waste disposal policies—did violate the Tenth

---

Morrison does not respond to the dissent's observation—most likely, because the states' willingness to surrender their powers is of no constitutional consequence.

338 505 U.S. 144 (1992).

339 Pub.L. 99-240, 99 Stat. 1842, 42 U.S.C. 2021b *et seq*.

340 For a colorful description of the states' and the NGA's agenda-setting role see *New York*, 505 U.S. at 189-194 (White, J., diss.).

Amendment. The provision, the Court reasoned, impermissibly "commandeered" the states' legislative process.

In reaching that conclusion, Justice O'Connor's opinion for the Court confronted the argument, pressed forcefully in a dissent written by Justice White,[341] that New York had consented to the statute, including its contested incentive provisions. In enacting the statute, Congress had merely "refereed" a process of state bargaining,[342] and New York's participation in that process over a period of many years "fairly indicate[d] its approval of the interstate agreement process"[343] embodied in the statute. In the dissenter's view, New York's belated resistance to the incentive provisions constituted an impermissible attempt to welsh on a deal that had gone sour for the state.

The majority rejected this argument on the ground that New York *could not consent* to the federal commandeering of its legislative process, because the Constitution does not grant Congress such a power. Explicitly analogizing the "consensual" transfer of state authority to the national government to the principles governing delegation in horizontal, separation of powers cases, the Court determined that "[s]tate officials … cannot consent to the enlargement of the powers of Congress beyond those enumerated in the Constitution."[344]

The application of this anti-delegation principle to the delegation of state authority to compact commissions is not altogether straightforward. First, the scope of the

---

341 *New York*, 505 at 188. The dissent was joined by Justice Blackmun and Justice Stevens, who also dissented separately.

342 *Id.* at 194.

343 *Id.* at 196.

344 *New York*, 505 U.S. at 182.

New York holding itself is unclear, and the broad statement just quoted cannot be quite right. For instance, while Congress lacks the power to abrogate state sovereign immunity under its Article I powers,[345] states may consent to such an abrogation by accepting federal funds, provided that the Spending Clause statute clearly state the congressional intent.[346] *New York* itself, in a different part of the majority opinion, explicitly declared federal "conditional spending" programs constitutionally unproblematic.[347] Second, *New York* can be read to suggest that states may delegate their sovereign power to anyone they want (including compact commissions)—except to the Congress.[348] The constitutional problem may be the augmentation of the powers of Congress, rather than the delegation of state sovereignty *per se*.

New York also suggests, however, that the enumerated powers doctrine and its anti-delegation logic occupy a central place in the larger constitutional architecture. In explaining the point of the anti-commandeering, anti-delegation principle, the *New York* Court articulated an accountability rationale: a "delegation" of state sovereignty to Congress would enable state officials to avoid political accountability for inconvenient decisions by "purport[ing] to submit to the direction of Congress."[349] *New York* rests on the recognition that "[t]he interests of public officials … may not coincide with the

---

345 *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996).

346 *Pennhurst State School & Hosp. v. Halderman*, 451 U.S. 1 (1981).

347 *New York*, 505 U.S. at 158-59.

348 *See, e.g., id.* at 182 ("*Where Congress exceeds its authority relative to the states*, … the departure from the constitutional plan cannot be ratified by the 'consent' of state officials." (emph. added)).

349 *Id.* at 183.

Constitution's intergovernmental allocation of authority."[350] Constitutional federalism, though, is not "for the benefit of public officials" but for citizens,[351] and citizens cannot avail themselves of federalism's protections if state officials are permitted to diffuse and obfuscate political responsibility in an end run around the constitutional forms.

The Supreme Court applied and extended the *New York* accountability rationale in several subsequent decisions,[352] and while its reach and the contours remain somewhat unclear,[353] an injunction against delegations of state sovereignty to compact commissions seems close to its core. It is true that the Supreme Court's federalism decisions indicate a pronounced respect for state autonomy, which is in large measure grounded in the belief that the states are—in the common phrase—"closer to the people," more accountable to them and more reflective of their diverse preferences, than the distant national government. Neither that respect, however, nor the presumption on which it is based, can possibly extend to state-created compact commissions.[354] It is likewise true that the Supreme Court's federalism reflects a preoccupation with the federal-state "balance," a consideration that may weigh against state delegations to Congress but for compact commissions as another line of defense against an overbearing national government. But if the accountability principle means anything at all, it must mean that delegations to

---

350 *Id.*

351 *Id*. at 181.

352 *See, e.g., Printz v. United States*, 521 U.S. 898 (1997); *Alden v. Maine*, 527 U.S. 706 (1999).

353 The accountability principle's uncertain reach and application have generated considerable academic criticism. *See, e.g.*, Evan H. Caminker, *Printz, State Sovereignty, and the Limits of Formalism*, 1997 SUP. CT. REV. 1999; Vicki C. Jackson*, Federalism and the Uses and Limits of Law: Printz and Principle?,* 111 HARV. L. REV. 2180 (1998); and William P. Marshall & Jason S. Cowart, *State Immunity, Political Accountability, and Alden v. Maine*, 75 NOTRE DAME L. REV. 1069 (2000).

354 Note, *Charting No Man's Land: Applying Jurisdictional and Choice of Law Doctrines to Interstate Compacts*, 111 HARV. L. REV. 1991, 1995 (1998).

extra-constitutional bodies created from whole cloth are far more problematic than a state-induced augmentation of congressional authority. To the extent that the Constitution leaves room for such bodies, their creation requires congressional approval under the Compact Clause.[355]

The Functional Compact Clause and the Real Thing. The functional Compact Clause test just sketched is faithful to the purpose and structure of the Compact Clause. Like the textual Compact Clause, it aims to establish an error-minimizing rule that guards against harmful state compacts, without unduly restricting fruitful and beneficial state cooperation. The functional test is more nuanced than the Compact Clause rule. It is more accommodating to "federalism" (in the primitive sense of uninhibited state activity), and it entails lower institutional transaction costs in the formation of compacts. Unlike the judicial enforcement of the Compact Clause, as written, the functional test accommodates the great majority of precedents.

Against these advantages weighs a powerful Madisonian objection. The intended benefits—a reduction of the states' bargaining costs—are likely small: risk-free state agreements are unlikely to prompt any more acrimony or delay than the congressional declaration of the National Dairy Goat Appreciation Week. The compacts that are bound to trigger argument and delay are the ones that ought to do so, on account of their consequences for sister-states or national concerns. On the other hand, the effort to strike

---

[355] For reasons mentioned *supra* nn. and accompanying text, congressional approval would ameliorate the accountability problem. It would not, however, solve the delegation problem. The congressional approval of a state compact commission and its exercise of delegated state powers is on a par with the congressional creation of such a commission and a direct congressional delegation of federal authority. The difficult questions of whether and to what extent such delegations are permissible are beyond the scope of this Article.

the constitutional balance just so invites an awful lot of confusion, argument, and abuse. A Compact Clause with a police power or reciprocity exemption resembles a requirement that all candidates for president must be 35 years of age, except for persons of uncommon maturity: though consistent with the purpose of the Clause, it undermines its operation. For example, Texas may grant Oklahoma students preferred access to its public universities, provided that Oklahoma extend comparable treatment to an equal number of Texans. While such an endeavor to expand citizen choice and to improve government efficiency (by expanding the applicant pool for educational fields with insufficient in-state demand) falls squarely within the states' domain, the compact may also be an attempt to subvert a judicial injunction against non-remedial racial preferences.[356] Well short of an outright violation of the Fourteenth Amendment, that would implicate the authority of Congress to enforce the provisions of the Amendment. A functional Compact Clause, though, invites the courts to police the boundaries. Relative to the actual Compact Clause, it both expands and complicates the judicial function. (Since a state compact designed to circumvent Fourteenth Amendment constraints will not declare that purpose but rather disguise it, the judicial inquiry will turn into a fact-intensive and error-prone examination.) That does not sound like a good idea. The courts have made hash even of the actual Compact Clause, who knows what they might do with a four-prong risk test.

---

[356] *Hopwood v. State of Texas*, 78 F.3d 932 (5th Cir. 1996), *cert. denied*, 518 U.S. 1033 (1996). The hypothetical is not entirely—well, hypothetical. A Southern Regional Education Compact in 1948 failed to obtain congressional approval because civil rights leaders, including Thurgood Marshall, feared that the compact was a ruse to escape federal anti-discrimination requirements. WELDON V. BARTON, INTERSTATE COMPACTS IN THE POLITICAL PROCESS 132-33 (1965). Marshall argued that the Compact did not require congressional approval: *unless* it were understood as a vehicle to perpetuate segregation, it did not involve national prerogatives.

The potential for state evasion, coupled with the difficulty of policing such evasion through the judiciary, explains why the Compact Clause does not contain a police power exception or any other qualification but rather applies to "*any* agreement or compact"—as Madison put it, to "any cases whatsoever." Its logic is at some level implacable. The most urgent task at hand, though, is to recapture the core purpose of the Compact Clause, and the functional test may do the job precisely because it does not restore the Clause to its original sweep and glory. Unlike the Founders, we cannot design the judicial function under the Compact Clause in accordance with its constitutional logic. Rather, we have a choice between a Compact Clause doctrine that reflects that function and logic, which the courts have messed up beyond repair; and a doctrine comports with modern precedents and prejudices, to the extent that this is possible without compromising core constitutional purposes. That more limited doctrine might help to direct the states' search for cooperative gains into areas where the national government's competence is most limited, and it may alleviate the fears over unwarranted federal interference that have contributed to the judiciary's Compact Clause inversion. The courts just might get the functional doctrine right. In the process, they might even take a meaningful step towards the reassertion of a more serious, more constitutional federalism. That cheerful prospect is examined below, immediately following the tying-up of a loose end.

C. A Brief Note on Congressional Consent

If state agreements require no congressional consent, the timing and form of consent are unlikely to become live issues. For that obvious reason, *Virginia v. Tennessee*

was the last case to address those questions directly.[357] A re-invigoration of the Compact Clause would invariably raise the question anew. The Clause itself supplies no answer, and the presumptions with which one might want to approach the question cut both ways. The logic of the Compact Clause dictates that consent must ordinarily precede a compact; antecedent approval of state arrangements, as distinct from *ex post* preemption, is the point of the Clause. Madison clearly intended the negative to operate *ex ante*, and in adopting the negative in a limited range of application, the Convention understood and accepted that interpretation.[358] Then again, the unequivocal commitment of all agreements and compacts to the Congress implies a case for some congressional license, and corresponding judicial deference, concerning the form and the timing of consent. Recognizing as much, the Supreme Court has held that congressional consent may be given after the fact and, moreover, may be implied, both for *ex ante* and *ex post* approval.[359] The most plausible and precedent-friendly way of reconciling the conflicting considerations is a rule that requires a clear statement of congressional intent at some point in the life of a compact or else, overwhelming evidence of congressional acquiescence.

The first, "clear statement" leg has a clear analogy: a clear statement is required for congressional validations of state activities that otherwise violate the negative

---

357 *Virginia v. Tennessee*, 148 U.S. 503, 521 (1893).

358 *Supra* nn. and sources cited *id.*

359 For implied approval *ex ante see, e.g., Northeast Bancorp v. Bd. Of Governors of Fed. Reserve*, 472 U.S. 159, 175-76 (1985) (possibly *dictum*). For implied approval after the fact *see Virginia v. Tennessee*, 148 U.S. 503, 521 (1893); *Virginia v. West Virginia*, 78 U.S. 39 (1878); *Green v. Biddle*, 21 U.S. (8 Wheat.) 1, 85-87 (1823).

Commerce Clause.[360] In that application, the clear statement rule reflects federalism's horizontal dimension: in applying the negative Commerce Clause, the Court acts, in the face of what looks like congressional abdication, as a line of defense against interstate exploitation. If Congress wishes to overrun that line, or if what looked to the Court like abdication was actually a form of active acquiescence, Congress must clearly say so. A clear statement rule for compact approval has the same structure and consequence, and it is particularly appropriate in that context. To the extent that the clear statement rule may seem somewhat suspect in the negative Commerce Clause setting, that is because the negative Commerce Clause itself is suspect. No such objection arises under the Compact Clause. The state enactments at issue are themselves suspect under the Constitution; they are not *made* suspect by a judicial construct.[361]

As noted, the Supreme Court has in the past inferred congressional approval even without a clear statement. These ancient rulings—issued without exception in cases involving state boundary compacts, where the courts viewed finality as supremely important[362]—do not readily yield a doctrine that fits the contemporary constitutional universe and compacts of a very different nature. The reach of the implied consent

---

360 *New York v. United States*, 505 U.S. 144, 171 (1992) (citing *Wyoming v. Oklahoma*, 502 U.S. 437, 458 (1992); *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 427-31 (1946)).

361 Similarly, in its application in the ordinary statutory context, the clear statement rule has been criticized as a form of surreptitious judicial nullification: it imposes such inordinate legislative transaction costs that congressional bargains—also known as legislation—often become impossible. *See, e.g.*, William Eskridge, *Overriding Supreme Court Statutory Interpretation Decisions*, 101 YALE L. J. 331, 409-414 (1991). That objection, too, is inapplicable in the Compact Clause setting, where affirmative legislation *ought* to be difficult and expensive.

362 The cases consistently emphasize the importance of clear and settled boundaries—recognized as vital under the law of nations—as a reason for recognizing congressional consent *ex post* and by implication. *See, e.g.*, *Virginia v. Tennessee*, 148 U.S. 503, 522-23 (1893); *Boyd v. Graves*, 17 U.S. 513, 517-18 (1819); *Rhode Island v. Massachusetts*, 37 U.S. 657, 734 (1838); *U.S. v. Stone*, 65 U.S. 525, 537 (1864).

exception is hard to discern, since no case presents an instance of congressional acquiescence that *failed* to constitute implied congressional consent. The facts of the cases, though, suggest a standard comparable to the contemporary judicial approach to congressional acquiescence to administrative interpretations of federal statutes: where such interpretations implicate constitutional questions concerning the outer limits of congressional authority, the Supreme Court will infer acquiescence only "with extreme care" and in the face of "overwhelming evidence."[363]

Consistent with this standard, implied consent cases under the Compact Clause uniformly presuppose that prior (and explicit) approval is the constitutional rule or baseline; otherwise, consent by implication would require no judicial explanation and justification at all. The exception for congressional approval after the fact covers (in dicta) emergencies[364] and (in holdings) instances in which the nature of the agreement does not permit of prior approval.[365] Uniformly, moreover, the judicial inference has been based on congressional actions that *necessarily* imply consent to a state agreement, such as the admission of a new state whose boundaries were earlier agreed upon by compact;[366] or on ample evidence showing that Congress affirmatively relied on a particular state agreement for a period spanning over a century.[367]

---

363 *Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159, 169 n.5 (2001). The approach is predicated on constitutional problems; barring such problems, administrative interpretations of ambiguous statutory language are entitled to judicial deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1987). For reasons that are not altogether evident, the *Solid Waste* Court applied both the "overwhelming evidence" and, *id.* at 172-74, the "clear statement" rule.

364 *See supra* nn.

365 *Virginia v. Tennessee*, 148 U.S. at 521xx "("[W]here the agreement relates to a matter which could not well be considered until its nature is fully developed, it is not perceived why the consent may not be subsequently given.")

366 *Green v. Biddle*, 21 U.S. (8 Wheat.) 1, 87 (1823); *Virginia v. West Virginia*, 78 U.S. 39, 60 (1878). See also STORY, COMMENTARIES ON THE CONSTITUTION sec. 1399 ([T]he consent of congress … is always

A rule requiring either a clear statement or else, overwhelming evidence of congressional consent would save neither the Multistate Tax Compact nor the Master Settlement Agreement: Congress has never explicitly consented to those arrangements, and the evidence of implied consent is decidedly underwhelming.[368] Such a result would certainly distress states and private interests that have come to rely on those arrangements. They should direct their complaints and concerns to the forum that the Constitution provides—the United States Congress.

VII. Compacts and the Constitution

Why does the Compact Clause matter? One obvious and perfectly plausible answer is that we ought to care about representative government. It is not a good thing to be regulated and governed by obscure, off-the-charts commissions somewhere between the states and the nation. Taxes should be levied by the legislative bodies that are authorized to do so. A decision to turn a major industry into public utility and to exact the monopoly rents from consumers should not be the private business of a handful of policy

---

to be implied, when congress adopts the particular act by sanctioning its objects, and aiding in enforcing them. Thus, where a state is admitted into the Union, notoriously upon a compact between it and the state, of which it previously composed a part; there the act of congress, admitting such state into the Union, is an implied consent to the terms of the compact."

367 *Virginia v. Tennessee*, 148 U.S. 503, 522-24 (1893).

368 Congress has occasionally acknowledged the MTC's existence and, for reasons of administrative convenience, relied on its standard-setting functions. *See, e.g.*, Mobile Telecommunications Souring Act, P.L. 106-252, **[stat cite]**. Such acts of convenience hardly amount to a clear statement of congressional approval, let alone overwhelming evidence of congressional acquiescence. Similarly, the federal government's decision to surrender its claims on the states' Medicaid recoupment under the MSA (*see* P.L. 106-31 (May 21, 1999), 113 Stat. 103 (amending Sec. 1903(d)(3) of the Social Security Act, 42 U.S.C. 1396b(d)(3)), constitutes only a (revocable) permission to use the funds in a particular fashion, not an acceptance of the MSA *per se*. The recitation of congressional purposes in the statute contains no suggestion of such an acceptance.

entrepreneurs and tobacco executives; it ought to be discussed and voted upon in an open, responsible fashion, in the bodies that are authorized to make such decisions.

The emasculation of the Compact Clause could wreak even more serious havoc than has already occurred. The Multistate Tax Compact may encourage states to extend tax cartels to new forms of interstate commerce, such as internet sales. The tobacco cartel might serve as a precedent for similar campaigns against gun manufacturers and other disfavored industries.[369] The permissive doctrines developed under the domestic Compact Clause may spill over into foreign affairs.[370] Harbingers of these developments are already upon us—insistent state demands for a compact-based "Streamlined Sales Tax Project" that would enable states to impose sales tax obligations on remote (internet or catalogue) sellers in foreign states;[371] attorneys general trolling for support for tobacco-style lawsuits;[372] state efforts to pursue a foreign policy of their own, at variance with the foreign policy of the *United* States.[373] Modern economic realities lend special force to these temptations. The greatly increased mobility of capital, labor, and business enterprises puts the states' budgets and their ability to control their own affairs under

---

369 The prediction is a staple in the literature. *See, e.g.*, Dagan & White, *Injurious Industries* at 355; Ayres, Tort Settlements, 34 VAL. U. L. REV. at 607-08; MICHAEL I. KRAUSS, FIRE AND SMOKE (2000)

370 Swaine, *Negotiating Federalism* at 1223 & *id.* n. 337 (articulating that fear).

371 *See, e.g.,* Jonathan Fried*, No Hype: Four Web Tools That Work and Save Money: of Marshmallows and Tax Agita*, N.Y. TIMES June 13, 2001, H-3.

372 *See, e.g.*, http://overlawyered.com/archives/99oct2.html#991026a (describing state attorney general proposal to sue lead paint and pigment makers in partnership with trial lawyers and to "go after" latex rubber industry for alleged health problems possibly caused by latex allergies) (visited Mar. 4, 2002).

373 *See, e.g., Natsios v. Foreign Trade Council*, 530 U.S. 363 (2000). *See also* Swaine, *Negotiating Federalism*, 49 DUKE L. J. at 1130-32; EARL H. FRY, THE EXPANDING ROLE OF STATE AND LOCAL GOVERNMENTS IN U.S. FOREIGN AFFAIRS (1998).

enormous pressure. Increasingly, states will respond to that pressure through cartel arrangements that trump interstate competition.

The case for rediscovering the Compact Clause, though, does not rest exclusively or even primarily on such dire predictions. Absurd precedents typically encounter cultural inhibitions and political obstacles before they play themselves out to their logical extremes. If those inhibitions and obstacles were to fall and fail—if, for instance, a state-supported trial lawyer campaign against the fast food industry were to garner the support of the *New York Times*, the U.S. Surgeon General, and the trial bar's congressional patrons[374]—the Compact Clause would not save us. Nothing would.

The case for rediscovering the Compact Clause, rather, lies in the hope of restoring a piece of constitutional order and argument. *U.S. Steel Corp. v. Multistate Tax Commission* is a pristine exhibit of free-form adjudication,[375] marked by a complete indifference to the constitutional text, logic, and architecture; tendentious readings of the precedents; and a ready resort to functional arguments that collapse under inspection. A judiciary that is seriously committed to constitutionalism could do worse than to clean out this particular constitutional corner.

In and of itself, such an endeavor might seem unattractive. Judicial time, prestige, and intellectual effort are scarce resources that may be invested most profitably in

---

[374] Everything that is true of cigarettes—harmful health effects, industry efforts to conceal those effects, consumer addiction, massive advertising and selective targeting of children—is also true of fast food. Any second-year associate in the country could find himself an obese grease addict and a trim, ambitious attorney general, download one of the state briefs in the tobacco litigation, substitute "hamburger" for "tobacco" and "McDonald's" for "RJR," and file the case. Obstacles to such cases exist, but none of them have to do with the law.

[375] The felicitous term is Professor Tribe's. *See* Lawrence H. Tribe, *Taking Text and Structure Seriously: Reflections on Free-Form Method in Constitutional Interpretation*, 108 HARV. L. REV. 1221 (1995).

revisiting doctrines and precedents that are central to the constitutional architecture and in addressing question that are bound to recur with some regularity. That consideration, however, cuts both ways. Precisely because the Compact Clause is a relatively isolated constitutional cubicle, it is more easily clean-outable than the Constitution's crammed main stables. If that can be accomplished, it may turn out that the brooms that work in the corners can, and should, sweep more broadly.

The restoration of constitutional, judicially enforceable federalism norms has been all accounts been the modern Supreme Court's central project. In the central arenas where federalism battles tend to be fought, though, the ground is strewn with paradoxes and unintended consequences,[376] and while it is not polite to say so, the Court must also take account of political realities and constraints. A full-scale reassertion of the Commerce Clause, for a ready example, can only be achieved in steps; an outright reversal of *Wickard v. Filburn*[377] or *United States v. Darby*[378] is out of the question. And so the Court has of needs gone about its federalism project through a kind of asymptotic approximation of constitutional norms. That strategy may be defensible as a form of judicial statesmanship. [379] Still, individual decisions will inevitably appear calculating, political, and perhaps even cynical. And while this or that particular decision may pass a

---

376 The difficulty can be traced in every major federalism decision of the past decade, and it has generated a respectable body of law review comment. *See, e.g*., Pamela Karlan, *The Irony of Immunity: The Eleventh Amendment, Irreparable Injury, and Section 1983*, 53 STAN. L. REV. 1311 (2001) (Supreme Court's Eleventh Amendment jurisprudence may prompt more rather than less judicial intrusion into state affairs); Adrian Vermeule, *Does Commerce Clause Review Have Perverse Effects?*, 46 VILL L. REV. 1325 (2001).

377 317 U.S. 111 (1942).

378 312 U.S. 100 (1941).

379 For my own modest stab at a "statesmanship" defense *see* MICHAEL S. GREVE, REAL FEDERALISM: WHY IT MATTERS, HOW IT COULD HAPPEN (1999).

straight-face test and, in any event, represent an improvement over the *status quo*, even that cannot be taken for granted.[380]

By way of illustrating the potential unintended consequences of piecemeal federalism, consider the post-New Deal preemption doctrines and presumptions. Arguably, the only form of preemption that naturally flows from the Supremacy Clause is what we now call "conflict preemption"; the rest of this messy universe is largely a nationalist invention, rather than a legitimate constitutional inference.[381] A great deal could be said for a return to a more originalist supremacy/preemption rule if we were operating within the larger constitutional structures of which that rule was a part—including, notably, a robust enumerated powers doctrine that ensures state competition and citizen choice and exit in areas beyond the national government's reach, along with choice-of-law rules that preclude states from regulating citizens and businesses in other states. These structures, however, collapsed six-plus decades ago. Post-*Wickard*, post-*Erie* and *Klaxon*,[382] the law permits virtually boundless state regulatory aggression against out-of-state citizens and, moreover, encourages a policy race between states and

---

380 For example, the rule of *United States v. Morrison*, 529 U.S. 598 (2000), distinguishing between "economic" conduct within the purview of the Commerce Clause and non-economic conduct that falls beyond that boundary, seems quite sensible. (For a sophisticated, pre-*Morrison* argument along these lines *see* Grant S. Nelson & Robert J. Pushaw, Jr., *Rethinking the Commerce Clause: Applying First Principles to Uphold Federal Commercial Regulations but Preserve State Control over Social Issues*, 85 IOWA L. REV. 1 (1999). However, the decision suggest that certain federal interventions that, standing alone, violate the Commerce Clause might yet be constitutional if they are an integral part of a larger regulatory scheme. That rule, paradoxically, may produce more centralization than no Commerce Clause review at all: Adrian Vermeule, *Does Commerce Clause Review Have Perverse Effects*? 46 VILL. L. REV. 1325 (2001). Vermeule's advice to the decentralizing judge is to change the subject. *Id.* at 1339. That advice is consistent with the argument here and in the remainder of this article.

381 *See, e.g.*, Caleb Nelson, *Preemption*, 86 VA. L. REV. 225 (2000).

382 *Erie Railroad v. Tompkins*, 304 U.S. 64 (1938); *Klaxon Co. v. Stentor Electric Mfr. Co*., 313 U.S. 487 (1941).

the national government towards ever-higher levels of regulation.[383] In that world, expansive preemption doctrines are the only backstop. They almost certainly help to preserve the constitutional balance, whereas originalism—without a concurrent but politically impossible adjustment elsewhere—would produce a wholesale commercial balkanization that is the precise opposite of the Founders' project.

The Compact Clause is much less likely to produce paradoxes and unintended consequences. The Clause is not a constitutional oddity or superfluous wrinkle; as I hope to have shown, it is an integral part of the constitutional logic and architecture. Compact Clause decisions reflect the intellectual errors and confusions that have afflicted federalism jurisprudence in general—wholesale disregard of federalism's horizontal, state-to-state dimension; cooperative enthusiasms that mask statist ambitions; the notion that increased social complexity demands greater tolerance for interest group rackets and political collusion. Unlike the Commerce Clause or preemption doctrines, however, the Compact Clause applies to a small, defined set of state activities. Rules and doctrines developed in this corner are more easily compartmentalized, and because that is so, it is easier to get them right.

Especially in the functional version I have attempted to defend, the Compact Clause offers an opportunity to work out and fortify the enumerated powers and accountability principles with which the Supreme Court has experimented in other, less easily cabined areas. It provides an opportunity to recognize that—and why—reciprocity among sister-states is consistent with federalism's dual commitments to political

[383] In contrast to horizontal, state-to-state policy competition, vertical competition is a one-directional race: each regulatory intervention, at whatever level, is only a floor for the next round of intervention at a different level. *Sans* preemption, the dynamic has no stopping point.

decentralization and a common market, whereas political coordination cartels are an affront to both.[384] Most important, perhaps, a reassertion of the Compact Clause must rest on a renewed recognition that federalism must mean state equality and integrity. A lack of attention to federalism's horizontal dimension is a sure-fire way of getting just about everything about federalism wrong, and the courts have managed to do so. A serious, constitutional federalism will ultimately require a re-thinking of the negative Commerce Clause;[385] a very different Spending Clause jurisprudence; [386] and a revision of the idea that the choice of state law is not a federal question.[387] Before embarking on such daunting ventures, though, 'tis best to reassert the constitutional principle in an area where it is less likely to trigger unexpected consequences. That re-assertion, moreover, would come more easily than a comparable exertion in areas that are cluttered with messy precedents: to all intents, Compact Clause jurisprudence consists of a single shoddy opinion.

Political considerations have in federalism's main arenas compelled the Supreme Court to aim its fire and largely symbolic statutes, such as the Gun Free School Zones Act.[388] In contrast, a Supreme Court decision to put the Multistate Tax Commission or,

---

384 For a powerful presentation of this argument see Wolfgang Kerber, *Rechtseinheitlichkeit und Rechtsvielfalt aus oekonomischer Sicht*, in, SYSTEMBILDUNG UND SYSTEMLUECKEN IN KERNGEBIETEN DER HARMONISIERUNG: EUROPAEISCHES SCHULDVERTRAGS- UND GESELLSCHAFTSRECHT 67 (S. Grundmann, ed., 1999). *See also* Kerber, *Interjurisdictional Competition within the European Union*, 23 FORDHAM INTL. L. J. 217 (2000).

385 *See supra* nn. and accompanying text.

386 *See supra* nn. and accompanying text.

387 For a powerful critique of that strange modern notion *see* Douglas Laycock, *Equal Citizens of Equal and Territorial States: The Constitutional Foundations of Choice of Law*, 92 COLUM. L. REV. 249 (1992).

388 *Lopez v. United States*, 514 U.S. 549 (1995). *See also United States v. Morrison*, 529 U.S. 598 (2000) (invalidating provision of the Violence Against Women Act). The perception that the Supreme

more likely, the Master Settlement Agreement out of its misery would strike at something real—without, at the same time, exposing the Court to a serious political backlash. Unlike a far-reaching ruling under, say, the Commerce Clause, a Compact Clause revival would neither sweep up a vast array of laws and arrangements *nor even be the final word on the matter*. Unlike federalism decisions that invite criticism on account of the Court's "activist" willingness to second-guess and confront the Congress and its corresponding insistence on judicial supremacy,[389] a constitutionalist ruling on the Compact Clause would send the opposite, deferential signal. Instead of choking off political deliberation, it would generate a public and congressional debate that we should have had before those monstrosities went into operation.

While the reassertion of serious federalism doctrines under the Compact Clause would have numerous advantages, the spread of those doctrines *beyond* that context would remain controllable. Even if litigants have the imagination to connect the dots between the a judicial re-discovery of a constitutional Compact Clause and, say, the Commerce Clause, judges and Justices may easily disavow or deny that connection. But they may also affirm and endorse it—at their own chosen speed, and under suitable conditions. For a Supreme Court that is running out of viable federalism options, the Compact Clause might prove a splendid vehicle and opportunity.

Court is targeting "symbolic" statutes in a tactical fashion has engendered criticisms of the Court's federalism jurisprudence as hypocritical and calculating. *See, e.g.*, Jeffrey Rosen, *Hyperactive*, THE NEW REPUBLIC Jan. 31, 2000, available at http://www.tnr.com/013100/rosen013100.html (visited Feb. 28, 2002).

[389] For thoughtful criticisms of this aspect of the Supreme Court's federalism *see* Michael McConnell, *Institutions and Interpretation: A critique of City of Boerne v. Flores*, 111 HARV. L. REV. 153 (1997); and Evan H. Caminker, *Appropriate Means-Ends Constraints on Section 5 Powers*, 53 STAN. L. REV. 1127 (2001).