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# FEDERALISM AND NATURAL RESOURCES

## PROLOGUE

James H. Goetz\*

### I.

“[F]ederalism as a viable constitutional principle . . . is moribund if it is not dead,” according to one constitutional scholar.<sup>1</sup> Another queries pointedly, “[D]oes federalism exist and does it matter?”<sup>2</sup> He concludes, equally as pointedly, that federalism is a legal fiction which makes little difference in the way our nation is governed,<sup>3</sup> but “since some lawyers appear to believe in it, we must, I suppose, concede that it exists.”<sup>4</sup> The premise of these writers, of course, is that the central government has achieved such an overriding hegemony over the states that the principle of federalism—the federal-state division of power<sup>5</sup>—is of little real importance.

Whatever the merits of this conclusion in other areas of law, federalism is not so easily dismissed in the area of natural resources. Since 1976, there have been ten significant decisions by the Supreme Court which have involved federalism principles and either natural resource or environmental protection issues.<sup>6</sup> Of these ten, four have been resolved in favor of state power and six against.<sup>7</sup> The State of Montana has been an important, albeit un-

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1. Kurland, *The Impotence of Reticence*, 1968 DUKE L.J. 619, 620.

2. Riker, *Six Books in Search of a Subject—or Does Federalism Exist and Does It Matter?*, 2 COMP. POLITICS 135 (1969).

3. *Id.* at 145-56.

4. *Id.* at 136. See generally Schirber, *Federalism and Legal Process: Historical and Contemporary Analysis of the American System*, 1980 LAW & SOC. REV. 663, 663-69.

5. L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* 17 (1978).

6. See *infra* note 7.

7. Those cases resolved in favor of state power include: *Commonwealth Edison Co. v. Montana*, 101 S. Ct. 2946 (1981) (at time of publication, U.S. cite available at 453 U.S. 609 (1981)); *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980); *Baldwin v. Fish & Game Comm'n of Montana*, 436 U.S. 371 (1978); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976). Those resolved against state power include: *New England Power Co. v. New Hampshire*, 102 S. Ct. 1096 (1982); *Hodel v. Virginia Surface Min. & Reclamation Ass'n*, 452 U.S. 264 (1981);

willing, participant in these developments, as evidenced in *Baldwin v. Fish and Game Commission of Montana*<sup>8</sup> and, most recently, *Commonwealth Edison Co. v. Montana*.<sup>9</sup>

Paralleling these recent developments in federalism has been a continuing attempt by the Supreme Court to deal with questions of Indian sovereignty.<sup>10</sup> Natural resource issues have likewise figured prominently in these disputes, which have ranged from taxation of reservation oil and gas to adjudication and regulation of reservation waters.<sup>11</sup> Because of their unique status as both wards of the federal government and sovereigns in their own right,<sup>12</sup> Indian tribes must make use of a hybrid federalism, in which policies of self-determination are pursued, by virtue of federal policy, against both the states and the federal government.<sup>13</sup>

Montana—rich in natural resources and with seven major Indian reservations within its borders—has a large stake in the outcome of these legal struggles, which attempt to delineate the boundaries of sovereign power. Montana, for example, collected almost \$34 million in coal severance revenues in fiscal year 1978 and expected to receive no less than \$40 million in fiscal year 1979,

*Hodel v. Indiana*, 452 U.S. 314 (1981); *Hughes v. Oklahoma*, 441 U.S. 322 (1979); *Philadelphia v. New Jersey*, 437 U.S. 617 (1978); *Hicklin v. Orbeck*, 437 U.S. 518 (1978).

8. 436 U.S. 371 (1978).

9. 101 S. Ct. 2946 (1981).

10. See, e.g., *Merrion v. Jicarilla Apache Tribe*, 102 S. Ct. 894 (1982); *Montana v. United States*, 450 U.S. 544 (1981); *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980); *Washington v. Confederated Tribes of the Colville Indian Reservation*, 447 U.S. 134 (1980).

11. See, e.g., *Merrion v. Jicarilla Apache Tribe*, 102 S. Ct. 894 (1982) (tribal severance tax on oil and gas); *Colville Confederated Tribes v. Walton*, 647 F.2d 42 (9th Cir. 1981), cert. denied, 102 S. Ct. 657 (1981) (quantification and regulation of Indian reserved water rights).

12. Compare *United States v. Kagama*, 118 U.S. 375, 383-85 (1886) with *Worcester v. Georgia*, 31 U.S. (6 Pet.) 515, 561 (1832).

13. It must be noted that while the Constitution restrains congressional power over the states, there is, of course, no such restraint on Congress in governing tribal affairs. Congress' control over the Indian within the tribal context is plenary, and therefore that relationship cannot be characterized as true federalism. On the other hand, the inherent, although limited, sovereignty of Indian tribes, recognized by treaty and federal policy, gives rise to a *de facto* federalism in which three sovereign entities—the tribes, states and federal government—must co-exist. See generally F. COHEN, HANDBOOK OF FEDERAL INDIAN LAW 122-26 (U.N.M. ed. 1971); *United States v. Sioux Nation*, 448 U.S. 371, 415 (1979) (quoting in part *United States v. Creek Nation*, 295 U.S. 103, 109-10 (1934) (footnote and citations omitted):

In every case where a taking of treaty-protected property is alleged, a reviewing court must recognize that tribal lands are subject to Congress' power to control and manage the tribe's affairs. But the court must also be cognizant that "this power to control and manage [is] not absolute. While extending to all appropriate measures for protecting and advancing the tribe, it [is] subject to limitations inhering in . . . a guardianship and to pertinent constitutional restrictions."

when the constitutionality of the severance tax was decided.<sup>14</sup> Likewise, the Supreme Court in *Baldwin* recognized that Montana's elk population is "one of the largest in the United States,"<sup>15</sup> and that the state consistently attracts the highest, or nearly the highest, number of non-resident hunters each year.<sup>16</sup> Similarly, Montana has a substantial interest in the outcome of natural resource issues on and off Indian reservations. At this time, it seems certain that the Supreme Court will decide whether Montana tribes must submit to state adjudication of their water rights—a result with a substantial effect on the state-wide adjudication process.<sup>17</sup> Regulation of adjudicated reservation water exists as a separate and equally important issue.<sup>18</sup> Then there are the conflicts of taxation authority over reservation deposits of coal, oil and gas.<sup>19</sup>

Montana, of course, has survived constitutional challenges to its non-resident hunting license and to its coal severance tax. It has also prevailed in asserting jurisdiction over the Bighorn River.<sup>20</sup> The controversies, however, are ongoing, and additional issues arise as fast as the cases are decided.<sup>21</sup> The present issue of the *Montana Law Review* is devoted largely to these questions of the exercise of power by competing sovereign entities—states, tribes and the federal government—in the context of natural resource regulation and environmental protection. The timeliness and pertinence is obvious, and there is no doubt that these questions will continue to be of critical importance to the Western states and their citizens.

## II.

The principle of federalism is found primarily in the interstate commerce clause of the United States Constitution. The clause provides that Congress shall have the power "[t]o regulate com-

14. Commonwealth Edison, 101 S. Ct. at 2966 (Blackmun, J., dissenting).

15. *Baldwin*, 436 U.S. at 374.

16. *Id.* at n.9.

17. See *Northern Cheyenne Tribe v. Adsit*, 688 F.2d 723 (9th Cir. 1982) (Montana tribes' reserved water rights may not be adjudicated in state court pursuant to statewide program of MONTANA CODE ANNOTATED [hereinafter cited as MCA] §§ 85-2-211 through -243 (1981)).

18. See, e.g., *Colville Confederated Tribes v. Walton*, 647 F.2d 42 (9th Cir. 1981), cert. denied, 102 S. Ct. 657 (1981).

19. See, e.g., *Crow Tribe of Indians v. Montana*, 650 F.2d 1104 (9th Cir. 1981), modified, 665 F.2d 1390 (1982) (state power to tax reservation coal).

20. *Montana v. United States*, 450 U.S. 544 (1981).

21. See, e.g., *Montana v. Johnson*, CV-81-26-BU (March 4, 1982) (Bonneville Power Authority must comply with substantive requirements of Montana's Major Facility Siting Act (MCA §§ 75-20-101 through -1205 (1981) in regard to powerline construction).

merce with foreign Nations, and among the several States, and with the Indian Tribes . . . .”<sup>22</sup> Recently, the interstate privileges and immunities clause<sup>23</sup> has emerged as an important supplemental provision relating to federalism. In *Hicklin v. Orbeck*,<sup>24</sup> the Supreme Court spoke of the “mutually reinforcing relationship between the Privileges and Immunities Clause of Art. IV, § 2, and the Commerce Clause—a relationship that stems from their common origin in the Fourth Article of the Articles of Confederation and their shared vision of federalism . . . .”<sup>25</sup> The commerce clause has traditionally played a dual role: it is a source of national power, and coupled with the supremacy clause,<sup>26</sup> it is an inherent limitation on state power, commonly referred to as “dormant” commerce clause power.<sup>27</sup> The interstate privileges and immunities clause, on the other hand, serves solely as a limitation on state power, essentially in situations where a state attempts to discriminate against non-residents.<sup>28</sup>

The bulk of recent litigation under the commerce clause falls under the dormant commerce clause rubric—in other words, what may a state do in the absence of federal occupation of the field?<sup>29</sup> Where Congress has acted, however, it has been settled, with one notable exception since the New Deal, that the courts will not restrain the exercise of that congressional power.<sup>30</sup> The exception is *National League of Cities v. Usery*,<sup>31</sup> in which the Supreme Court held that the Federal Fair Labor Standards Act<sup>32</sup> could not be applied to the states. The Court observed that “there are attributes of sovereignty attaching to every state government which may not be impaired by Congress, not because Congress may lack an affirmative grant of legislative authority to reach the matter, but because

22. U.S. CONST. art. I, § 8, cl. 3.

23. U.S. CONST. art. IV, § 2.

24. 437 U.S. 518 (1977).

25. *Id.* at 531-32 (footnote omitted).

26. U.S. CONST. art. VI, § 2. Compare *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937) (source of federal power) with *Southern Pacific Co. v. Arizona*, 325 U.S. 761 (1945) (limitation on state power).

27. See generally, Anson and Schenkkan, *Federalism, The Dormant Commerce Clause, and State-Owned Resources*, 59 TEX. L. REV. 71 (1980).

28. See, e.g., *Hicklin*, 437 U.S. at 523-26.

29. See *New England Power Co. v. New Hampshire*, 102 S. Ct. 1096 (1982); *Commonwealth Edison Co. v. Montana*, 101 S. Ct. 2946 (1981); *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980); *Hughes v. Oklahoma*, 441 U.S. 322 (1979); *Philadelphia v. New Jersey*, 437 U.S. 617 (1978).

30. See, e.g., *Wickard v. Filburn*, 317 U.S. 111 (1942); *United States v. Darby*, 312 U.S. 100 (1941); *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937).

31. 426 U.S. 833 (1975).

32. 29 U.S.C. §§ 201-219 (1976).

the Constitution prohibits it from exercising the authority in that manner."<sup>33</sup> The Court's decision in *National League of Cities* gave rise to the expectation of a "new federalism," by which the continued expansion of federal power would be checked.<sup>34</sup> Like Professor Lopach in his article,<sup>35</sup> I feel that the significance of *National League of Cities* has been overestimated. The test laid down in that decision is too vague to be of use: the federal government may not take action that would threaten the states' "separate and independent existence"<sup>36</sup> or impair their "ability to function effectively within a federal system."<sup>37</sup> I feel that *National League of Cities* is an aberration, which will be of little value in curbing the extension of federal power where Congress chooses to act. This conclusion is borne out by the Court's decision in *Hodel v. Virginia Mining and Reclamation Association, Inc.*,<sup>38</sup> which affirmed the power of Congress, under the commerce clause, to implement the Surface Mining Control and Reclamation Act of 1977,<sup>39</sup> and rejected the application of *National League of Cities* because the Act did not regulate the states *qua* states.<sup>40</sup>

A menacing recognition of the plenary power of Congress is found in the concurring opinion of Justice White in *Commonwealth Edison*. Justice White reluctantly sided with the majority to uphold Montana's severance tax, but added, "This is a very troublesome case for me, and I join the Court's opinion with considerable doubt and with the realization that Montana's levy on consumers and other states may in the long run prove to be an intolerable and unacceptable burden on commerce."<sup>41</sup> The Justice, however, counseled withholding the Court's hand, "at least for now," recognizing that Congress possesses adequate power to remedy the situation at any time:

Congress has the power to protect interstate commerce from intolerable or even undesirable burdens. It is also very much aware of the nation's energy needs, of the Montana tax and of the trend

33. *National League of Cities*, 426 U.S. at 845.

34. See, e.g., Matsumoto, *National League of Cities—From Footnote to Holding—State Immunity From Commerce Clause Regulation*, 1977 ARIZ. ST. L.J. 35 (one of the many commentaries that sprang up in the wake of the decision).

35. Lopach, *The New Federalism of the Supreme Court: Diminished Expectations of National League of Cities*, 43 MONT. L. REV. 181 (1982).

36. *National League of Cities*, 426 U.S. at 851 (quoting *Coyle v. Oklahoma*, 221 U.S. 559, 580 (1911)).

37. *Id.* at 852 (quoting *Fry v. United States*, 421 U.S. 542, 547 n.7 (1975)).

38. 452 U.S. 264 (1981).

39. 30 U.S.C. §§ 1201-1328 (Supp. III 1979).

40. *National League of Cities*, 452 U.S. at 283-93.

41. *Commonwealth Edison*, 101 S. Ct. at 2964 (White, J., concurring).

in the energy-rich states to aggrandize their position and perhaps lessen the tax burden on their own citizens by imposing unusually high taxes on mineral extraction.<sup>42</sup>

Implicit in this concurrence, and in most of the decisions of the Court dealing with the commerce clause as a source of federal power, is the recognition that Congress may limit the extent of state severance taxes if it chooses. *National League of Cities* notwithstanding, Montana's coal severance tax faces a difficult time if Congress chooses to impose a statutory ceiling.

Although the power of Congress is plenary where it chooses to act, it is quite a different matter where Congress fails to act. In the absence of congressional action, states stand a good chance of maintaining their own power to regulate in a particular area. The test was set forth by the Supreme Court in *Pike v. Bruce Church, Inc.*:<sup>43</sup>

[T]he general rule . . . can be phrased as follows: Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits . . . . If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and whether it could be promoted as well with the lesser impact on interstate activities.

Just this term, the Supreme Court invalidated a 1913 New Hampshire statute that prohibits a corporation, which generates electricity by water power, from transmitting that energy out of state unless the New Hampshire Public Utilities Commission first approves.<sup>44</sup> The Court observed, "Our cases consistently have held that the Commerce Clause of the Constitution . . . precludes a State from mandating that its residents be given a preferred right of access, over out-of-state consumers, to natural resources located within its borders or to the products derived therefrom."<sup>45</sup> There are exceptions to this general rule. For example, where the state acts as owner or proprietor, the Court has been very tolerant of discrimination against non-residents.<sup>46</sup> Moreover, in *Common-*

42. *Id.*

43. 397 U.S. 137, 142 (1969) (citation omitted).

44. *New England Power Co. v. New Hampshire*, 102 S. Ct. 1096 (1982).

45. *Id.* at 1100 (citations omitted).

46. *See, e.g., Reeves, Inc. v. Stake*, 447 U.S. 429 (1980); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976).

*wealth Edison*, the court refused to find that Montana's tax discriminates against interstate commerce even though 90 percent of the coal was shipped to other states under contracts that shift the tax burden to non-resident utilities, and therefore, to citizens of other states.<sup>47</sup> In explanation, the Court observed:

But the Montana tax is computed at the same rate regardless of the final destination of the coal, and there is no suggestion here that the tax is administered in a manner that departs from this evenhanded formula. We are not, therefore, confronted here with the type of differential tax treatment of interstate and intrastate commerce that the Court has found in other "discrimination" cases.<sup>48</sup>

Likewise, the Court was even more tolerant in *Baldwin*, upholding a big-game hunting license fee, which appellants charged discriminated against non-residents and which the district court had found unjustified by any of the economic bases advanced by the state.<sup>49</sup> While diverse factual situations make a reconciliation of these holdings difficult and probably unproductive, it can be concluded that states may well continue to enjoy a wide latitude in enacting legislation dealing with natural resources. However, in the absence of more precise indicia from the Court, states are left with only a rough and rather mercurial guideline for enacting natural resource regulatory legislation: (1) the regulation may not blatantly discriminate against non-residents; (2) the impact of the legislation on interstate commerce may not be severe; and (3) the regulation must be based on legitimate local purposes.

### III.

*Commonwealth Edison* provides some indication of the leeway states may have in future dormant commerce clause challenges. In this case, Commonwealth Edison Co. tried to invoke the "fair share" theory in attacking the rate of the tax. That is to say, the utility admitted that a non-resident corporation, engaged in interstate commerce and doing business in Montana, could be compelled to pay taxes to Montana, but only its fair share.<sup>50</sup> The utility sought to invoke the fourth prong of the test set out in *Complete Auto Transit v. Brady*,<sup>51</sup> that the measure of the tax be

47. *Commonwealth Edison*, 101 S. Ct. at 2954.

48. *Id.* (citations omitted).

49. *See Baldwin*, 436 U.S. at 390-91.

50. *Commonwealth Edison*, 101 S. Ct. at 2955.

51. 430 U.S. 274, 279 (1977), *cited in Commonwealth Edison*, 101 S. Ct. at 2955.

reasonably related to the extent of the contact with the state.

As Mike McGrath and Walter Hellerstein point out in their article,<sup>52</sup> Montana successfully argued that the Supreme Court is institutionally ill-suited to decide the rate of the tax. The majority of the Court agreed: "The simple fact is that the appropriate level of rate of taxation is essentially a matter for legislative and not judicial, resolution."<sup>53</sup> The majority, however, also addressed the fourth prong of the *Complete Auto* test, stating:

The "operating incidence" of the tax . . . is on the mining of coal within Montana. Because it is measured as a percentage of the value of the coal taken, the Montana tax is in "proper proportion" to appellants' activities within the State and, therefore, to their "consequent enjoyment of the opportunities and protections which the State has afforded" in connection with those activities . . . .<sup>54</sup>

As Justice Blackmun effectively argues in dissent, this approach emasculates the true meaning of the *Complete Auto* test, which is designed to insure that non-resident persons doing business in a host state not be forced into an inordinate subsidization of the services offered by the host state.<sup>55</sup>

While Justice Blackmun effectively counters the majority's treatment of the *Complete Auto* test, it is interesting to note that neither the majority opinion nor the dissent addresses the more fundamental question—this is, whether the *Complete Auto* test is even applicable in a natural resources context. The *Complete Auto* test was derived to address regular commercial activities conducted by non-resident corporations in a host state. A different question is posed when finite natural resources of a host state are involved. In such cases, the state should be free to use the taxing mechanism to regulate the pace of development and to accomplish conservation as long as there is no discrimination against interstate commerce. For example, it is quite possible that the Montana legislature set the coal severance tax as high as it did in part because it wanted to slow the pace of coal development. As long as the coal is marketed both in-state and out-of-state, as Montana's coal is, there is no reason why Montana should not be able to assess a high severance tax. If the tax is used, at least in part, to regulate the pace of development, both as a conservation device and as a device to even

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52. McGrath and Hellerstein, *Reflections on Commonwealth Edison Co. v. Montana*, 43 MONT. L. REV. 165 (1982).

53. *Commonwealth Edison*, 101 S. Ct. at 2959 (footnote and citations omitted).

54. *Id.* at 2958-59 (citations omitted).

55. *Id.* at 2968-71 (Blackmun, J., dissenting).

the socio-economic impacts of development, then the fourth prong of the *Complete Auto* test<sup>56</sup> seems inapplicable. Moreover, a portion of Montana's revenue from the coal severance tax is put in trust for future generations to buffer the impacts when the coal runs out. Given that purpose, which seems to be an entirely legitimate local interest, the fair share approach of the *Complete Auto* test seems even more inappropriate.<sup>57</sup>

In future natural resources cases involving federalism principles, states are likely to become increasingly sophisticated in advancing legitimate local interests to justify the impacts on interstate commerce. As long as the states can avoid blatant discrimination against non-residents, and as long as they can carry enough political clout with Congress to keep the federal government from actively legislating, it appears that states will play a viable role in the control of natural resource development.

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56. That test may be summarized as whether the non-residents share of taxes is reasonably related to services rendered. *Complete Auto*, 430 U.S. at 279.

57. See *Baldwin*, 436 U.S. at 390 (some support for this rationale in terms of equal protection analysis): "The legislative choice was an economic means not unreasonably related to the preservation of a finite resource and a substantial regulatory interest of the state."

