NOTE

Applying the Market Participant Exception to Selective Purchasing Laws That Affect Foreign Commerce Relations: Reading Between the Lines of *National Foreign Trade Council v. Natsios*

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On June 19, 2000, the United States Supreme Court decided the case of *Crosby v. National Foreign Trade Council*.[1] Affirming the First Circuit's decision in *National Foreign Trade Council v. Natsios*,[2] the Supreme Court in *Crosby* held that the "Massachusetts Burma Law,"[3] a Massachusetts selective purchasing law, was unconstitutional because it violated the Supremacy Clause of the United States Constitution[4].

The Massachusetts legislature enacted the Burma Law in 1996 to condemn the human rights violations occurring in Myanmar (formally Burma).[5] The law essentially prohibited the state from contracting with businesses that "do business with Burma."[6]

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1. 530 U.S. 363 (2000).
2. 181 F.3d 38 (1st Cir. 1999).
3. MASS. GEN. LAWS ch. 7, §§ 22G-22M (1996).
4. The Supremacy Clause provides as follows:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. CONST. art. VI, § 2.

5. *Natsios*, 181 F.3d at 46-47. Burma is now called "Myanmar," but for purposes of this Note, I will use the name "Burma," as the courts and the parties involved in this suit chose to do so.
6. *Natsios*, 181 F.3d at 44.

In *Natsios*, the National Foreign Trade Council (NFTC), a coalition of business groups, alleged that the Massachusetts Burma Law was unconstitutional because it (1) violated the Supremacy Clause;[7] (2) violated the Foreign Commerce Clause;[8] and (3) unconstitutionally interfered with the foreign affairs power[9] of the federal government. The First Circuit agreed with NFTC, holding that the law was unconstitutional on all three grounds.[10]

The Supreme Court granted *certiorari* and, relying exclusively on the Supremacy Clause, held that the Massachusetts law was unconstitutional.[11] In doing so, the Supreme Court wrongly left unresolved the question of whether the "market participant exception" to the dormant Commerce Clause can be applied to allow a state to freely exclude business partners that it finds objectionable.[12] Rather, the Court should have held that when acting in the role of a market participant, a government is allowed to choose its own business partners, regardless of whether its choice is based on a moral or economic reason, and regardless of whether the business partners are foreign or domestic.[13] Such a holding is supported by the justifications for the market participant exception, a judicially created doctrine imposed to limit the reach of the dormant Commerce Clause. These justifications, including fairness and a need to avoid interference with state autonomy, apply consistently to transactions in both domestic and foreign commerce.[14]

In this Note, I will examine the background of the situation in Burma as well as the federal and state legislation passed in response to the atrocities occurring within Burma's borders. I will then address the First Circuit's holding that the Massachusetts Burma Law is unconstitutional, focusing on the court's foreign Commerce Clause analysis and failure to apply the market participant exception. Finally, I will discuss the history of and the justifications for the market

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7. U.S. CONST. art. VI, cl. 2.

8. U.S. CONST. art. I, § 8, cl. 3.

9. The federal government's foreign affairs power is not mentioned expressly in the text of the Constitution. Rather, it is "derived from the structure of the Constitution an the nature of federalism." Gerling Global Reinsurance Corp. v. Low, 240 F.3d 739, 751-52 (9th Cir. 2001) (citing Harold G. Maier, *Preemption of State Law: A Recommended Analysis*, 83 AM. J. INT'L L. 832, 836-37 (1989)).

10. *See generally Natsios*, 181 F.3d 38.

11. Crosby v. National Foreign Trade Council, 530 U.S. 363, 388 (2000).

12. In *Natsios*, the First Circuit addressed all three arguments raised by NFTC. For this reason, most of this Note will discuss the First Circuit's opinion in the *Natsios* case.

13. Unless, of course, a reason for exclusion rests on the basis of discrimination against a protected class, or, if in exclusion, the government is somehow denying a fundamental right.

14. *See generally* Dan T. Coenen, *Untangling the Market-Participant Exemption to the Dormant Commerce Clause*, 88 MICH. L. REV. 395 (1989).

participant exception, exploring how the exception should be applied in the context of foreign commerce.

In my analysis, I will focus on the dormant Commerce Clause and the market participant exception because of the implications these doctrines may have for future situations. For example, would a state or local government be barred from passing a selective purchasing law if there were no preemptive federal law involved? The outcome of such a case may depend on a proper application of the dormant Commerce Clause and the market participant exception. The courts have not yet decided this issue, but it is almost certain to arise in the near future, especially as markets become increasingly globalized.

I. BACKGROUND

A. Human Rights Violations in Burma

Situated in Southeast Asia, Burma is bordered by China, Laos, Thailand, and India. The British colonized Burma in 1886, and it later gained independence in 1948.[15] Burma enjoyed a brief period of parliamentary democracy until 1962, when the military, under General Ne Win, took power, and the Burma Socialist Programme Party (BSPP) became the official party of the new government.[16] Under Ne Win's control, Burma entered a period of isolationism. Ne Win rejected investments by Western and other foreign governments and nationalized Burmese banks, the import/export trade, and retail and industrial businesses.[17] During Ne Win's military reign, the Burmese economy collapsed.[18] By 1987, Burma had gone from being the "rice bowl of Asia" to the United Nation's "Least Developed Country."[19]

By 1988, economic stagnation and the suppression of political freedom transformed general discontent into a nationwide mass movement.[20] As a result of this movement, the military, in September of 1988, announced a coup and established the State Law and Order

15. International Labour Organization, *Report of the Commission of Inquiry Appointed Under Article 26 of the Constitution of the International Labour Organization to Examine the Observance by Myanmar of the Forced Labour Convention*, 1930 (No. 29) (July 2, 1998) <http://www.ilo.org/public/english/standards/relm/gb/docs/gb273/myanmar.htm> [hereinafter ILO Report].

16. *Id.*

17. *Id.*

18. *Id.*

19. *Id.*

20. *Id.* Aung San Suu Kyi, daughter of independence leader Aung San, emerged as the leader of this movement.

Restoration Council (SLORC).[21] Under the SLORC regime, the sociopolitical atmosphere in Burma continued to deteriorate.[22]

A 1996 International Labor Organization (ILO) report confirms that under SLORC rule, Burmese authorities forced the men, women and children of Burma to carry out a variety of labor-intensive tasks.[23] Not only did the authorities fail to compensate these workers, but they also subjected them to various forms of verbal, sexual, and physical abuse including rape, torture, and death.[24] Harsh penalties were imposed for any failure to comply with forced labor:

> Punishments included detention at the army camp, often in leg-stocks or in a pit in the ground, commonly accompanied by beatings and other forms of torture, as well as deprivation of food, water, medical attention and other basic rights. Women were subject to rape and other forms of sexual abuse at such times.[25]

While forced labor has existed in Burma since at least 1988, the use of forced labor for infrastructure-related projects appears to have been much less common before 1992.[26] However, in recent years, an increasing number of Burmese have been subjected to forced labor.[27] In 1995, Human Rights Watch/Asia estimated that from 1992 to 1995, at least two million people were forced to work on the construction of roads, railways, and bridges without pay.[28] Additionally, the government forced civilians to work on a variety of projects undertaken by Burmese authorities. It appears that these projects, which included the cultivation and production of goods, were undertaken for income-generation purposes.[29] Many of these goods were traded on the international market.[30]

A second atrocity that is closely related to the increase in forced labor is a pattern of unsustainable overuse of natural resources.[31] Along with its exploitation of the Burmese people, the Burmese government is attempting to fully exploit a substantial quantity of mineral, fishing, and timber resources, resulting in widespread

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21. *Id.*
22. Even though, in the spring of 1990, a tightly controlled election would have ended the military coup's rise to power, the military declared the election void and continued to rule.
23. ILO Report, *supra* note 15.
24. *Id.*
25. *Id.*
26. *Id.*
27. *Id.*
28. *Id.*
29. *Id.*
30. *Id.*
31. *Id.*

ecological devastation.[32] Many of these resources are incorporated into products that filter into international markets.[33]

Both of these atrocities, forced labor and the exploitation of natural resources, continue to occur in Burma, and the Burmese people continue to suffer. With little hope of assistance from within Burmese borders, it has become clear that the Burmese people need outside assistance and support. In response to these atrocities, Massachusetts took action and passed its Burma Law.

B. Federal Legislative Response to Burmese Human Rights Violations

Massachusetts was not alone in responding the human rights violations in Burma. Congress, during the Clinton administration, imposed sanctions on Burma three months after Massachusetts passed its law.[34] The federal legislation authorizing the sanctions includes five components: (1) it bars any United States assistance to the Government of Burma except for certain types of humanitarian assistance; (2) it authorizes the President to impose conditional sanctions by means of an executive order; (3) it instructs the President to work with members of the Association of South-East Asian Nations (ASEAN) and other countries having major trading and investment interest in Burma to develop a comprehensive, multilateral strategy to bring democracy to Burma and improve human rights practices and the quality of life for its people; (4) it instructs the President to report to Congress on conditions in Burma and on progress made in furthering a multilateral strategy; and (5) it grants the President the power to waive any of the sanctions if he or she determines and certifies to Congress that the application of such sanctions would be contrary to the national security interests of the United States.[35]

In May 1997, President Clinton issued an Executive Order pursuant to the Federal Burma Laws imposing trade sanctions on Burma.[36]

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32. *Id.*

33. *Id.*

34. National Foreign Trade Council v. Natsios, 181 F.3d 38, 47 (1st Cir. 1999).

35. *See* Exec. Order No. 13,047, 62 F.R. 28,301 (1997), *reprinted as amended in* 50 U.S.C. § 1701 (Supp. 1997).

36. *Natsios*, 181 F.3d at 48. *See* Exec. Order No. 13,047, 62 F.R. 28,301 (1997), *reprinted as amended in* 50 U.S.C. § 1701 (Supp. 1997). In *Natsios*, the National Foreign Trade Council asserted that these federally imposed trade sanctions preempted the Massachusetts Burma Law, and that the law thus violated the Supremacy Clause. Although this preemption argument may have some validity, this Note will not focus on this issue.

II. FACTS, PROCEDURAL HISTORY AND HOLDING IN *NATIONAL FOREIGN TRADE COUNCIL V. NATSIOS*

A. Facts

In 1996, Massachusetts enacted "An Act Regulating State Contracts with Companies Doing Business with or in Burma (Myanmar)," which popularly became known as the Massachusetts Burma Law.[37] In effect, the law prohibited Massachusetts and its agents from purchasing goods or services from anyone doing business with Burma.[38] It did this by authorizing the Operational Services Division (OSD), an agency within Massachusetts' Executive Office of Administration and Finance, to establish a "restricted purchase list."[39] This list was formed through an administrative process in which the OSD would make a preliminary finding that a company was "doing business with Burma," as defined by statute.[40] A company added to the preliminary list would then be provided an opportunity to submit a sworn affidavit to refute the finding.[41] Finally, the OSD would make a final decision whether to place that company on the restricted purchase list.[42]

If a company were placed on the list, Massachusetts would be prohibited from procuring goods or services from that company,

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37. *Natsios*, 181 F.3d at 45.

38. National Foreign Trade Council v. Baker, 26 F. Supp. 2d 287, 289 (D. Mass. 1998). The law defined "state agency" to include "all awarding authorities of the commonwealth, including, but not limited to, all executive offices, agencies, departments, commissions, and public institutions of higher education, and any office, department or division of the judiciary." MASS. GEN. LAWS ch. 7, § 22G (1996).

39. *Baker*, 26 F. Supp. 2d at 289.

40. *Id.*

Section 22 G defines "Doing Business with Burma" as:

> (a) having a principal place of business, place of incorporation or its corporate headquarters in Burma (Myanmar) or having any operations, leases, franchises, majority-owned subsidiaries, distribution agreements, or any other similar agreements in Burma, or being a majority owned subsidiary, licensee or franchise of such a person;
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> (b) providing financial services to the government of Burma (Myanmar), including providing direct loans, underwriting government securities, providing any consulting advice or assistance, providing brokerage services, acting as a trustee or escrow agent, or otherwise acting as an agent pursuant to a contractual agreement;
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> (c) promoting the importation or sale of gems, timber, oil gas or other related products, commerce in which is largely controlled by the government of Burma (Myanmar), from Burma (Myanmar);
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> (d) providing any goods or services to the government of Burma (Myanmar).

MASS. GEN. LAWS ch. 7, § 22G (1996).

41. *Baker*, 26 F. Supp. 2d at 289.

42. *Id.*

unless one of the statutory exceptions was available.[43] The first exception included situations in which the "procurement [was] essential" and the restriction "would eliminate the only bid or offer, or would result in inadequate competition."[44] The second exception involved the purchase by Massachusetts of certain medical supplies.[45] The final exception involved situations in which "there is no comparable low bid or offer."[46] These exceptions, however, occurred infrequently.

The Massachusetts Burma Law had significant effects. There were 346 companies, including forty-four American companies, on the restricted purchase list at the time NFTC filed its complaint in federal court alleging that the law was unconstitutional.[47] At least three of these companies stopped doing business in Burma as a result of the law.[48] The law also had a snowballing effect: at least nineteen municipal governments have subsequently enacted similar restrictive purchasing laws.[49]

In addition to the NFTC lawsuit, the Burma Law generated protests from a number of international trading partners, including ASEAN, Japan, and the European Communities (EC).[50] The latter two entities filed a complaint with the World Trade Organization's dispute review panel.[51]

Although the statute itself is not explicit about its purpose, an examination of the legislative history of the act reveals the intent of the Massachusetts legislature.[52] While introducing the bill that became the Massachusetts Burma Law, Representative Byron Rushing, the bill's sponsor, stated that the "identifiable goal" of the law was "free democratic elections in Burma."[53] Additionally, when Massachusetts' then Lieutenant Governor Paul Cellucci signed the bill, he made a statement that clearly outlined the purpose of the legislation:

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43. *Id.*

44. *Id.* § 22H (1996).

45. MASS. GEN. LAWS ch. 7, § 22I (1996).

46. *Id.* § 22G (1996). A "comparable low bid," is statutorily defined as one that is up to ten percent higher than a bid from a company on the restricted list.

47. National Foreign Trade Council v. Natsios, 181 F.3d 38, 47 (1st Cir. 1999).

48. *Id.* A number of companies have withdrawn from Burma in recent years. At least three of these companies cited the Massachusetts law as one of the reasons for their withdrawal.

49. *Id.* Some of these analogous laws affect nations other than Burma, including China, Cuba, and Nigeria. Massachusetts, however, is the first and only state government to enact such a law.

50. *Id.*

51. *Supreme Court Review of "Burma Law" will Decide Local Sanction Power*, AGENCE FRANCE PRESSE, Nov. 30, 1999.

52. National Foreign Trade Council v. Natsios, 181 F.3d 38, 46 (1st Cir. 1999).

53. *Id.*

> [D]ue to a steady flow of foreign investments, including those of some United States companies, [the] brutal military regime [in Burma] has been able to supply itself with weapons and portray itself as the legitimate government of Burma. Today is the day we call their bluff.[54]

Massachusetts' then Governor, William Weld, made an additional comment that "one law passed by one state will not end the suffering and oppression of the people of Burma, but it is my hope that other states and Congress will follow our example, and make a stand for the cause of freedom and democracy around the world."[55] Finally, Massachusetts clearly identified the purpose of the legislation in its response to the NFTC complaint, asserting to the district court that the law "expresses the Commonwealth's own disapproval of the violations of human rights committed by the Burmese government" and "contributes to the growing effort . . . to apply indirect economic pressure against the Burma regime for reform."[56] Massachusetts also argued that the law reflected "the historic concerns of the citizens of Massachusetts with supporting the rights of people around the world."[57] Massachusetts did not argue that the law was designed to provide any economic benefit to the state.[58]

Although the purpose of the law is clear, whether it violates the Foreign Commerce Clause remains in dispute and will be the topic of discussion for the remainder of this Note.

B. Procedural History

NFTC is a nonprofit corporation that represents member companies that engage in foreign trade.[59] It filed suit on April 30, 1998, in the United States District Court for the District of Massachusetts, seeking both declaratory and injunctive relief against the Secretary of Administration and Finance and the State Purchasing Agent for the Commonwealth of Massachusetts.[60] NFTC made three initial arguments: (1) the Massachusetts Burma Law unconstitutionally infringed on the federal government's foreign

54. *Id.*
55. *Id.*
56. *Id.*
57. *Id.*
58. *Id.* at 46-47.
59. *Id.* at 48. The First Circuit pointed out that thirty-four NFTC members are on the "restricted purchase list."
60. *Id.* at 48. The Secretary at the time of the original suit was Charles D. Baker, who was subsequently replaced by Frederick Laskey, who was subsequently replaced by Andrew S. Natsios, the Secretary at the time the appeal was made.

affairs power;[61] (2) the statute was invalid because federal law preempted the Massachusetts law; and (3) the law violated the Foreign Commerce Clause.[62]

The district court held that the Massachusetts Burma Law unconstitutionally infringed on the foreign affairs power of the federal government and, accordingly, granted declaratory and injunctive relief.[63] It did not consider NFTC's argument that the Massachusetts law violated the Foreign Commerce Clause.[64] The district court did find, however, that NFTC "[did] not [meet] its burden of showing that the Federal Burma Law preempted the Massachusetts Burma Law."[65]

Massachusetts appealed, and the case came before the First Circuit in June of 1999.[66] The First Circuit upheld the district court's holding that the Massachusetts law violated the Constitution.[67] Unlike the district court, however, the First Circuit addressed all three of NFTC's arguments. It affirmed the district court's finding that the Massachusetts Burma Law unconstitutionally interfered with the foreign affairs power of the federal government.[68] It also held that the Massachusetts Burma Law violated the Foreign Commerce Clause and the Supremacy Clause.[69]

Massachusetts petitioned for certiorari, which the Supreme Court granted on November 29, 1999.[70] The Supreme Court affirmed the First Circuit's holding that the Massachusetts Burma Law was unconstitutional on the basis of the Supremacy Clause.[71] The Court did not, however, address the other arguments raised by NFTC, including the dormant Commerce Clause argument and Massachusetts' market participant exception counter-argument:

> Because our conclusion that the state Act conflicts with federal law is sufficient to affirm the judgment below, we decline to speak to field preemption as a separate issue, or to pass on the First Circuit's rulings addressing the foreign affairs power or the dormant Foreign Commerce Clause.[72]

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61. National Foreign Trade Council v. Baker, 26 F. Supp. 2d 287, 291-93 (D. Mass. 1998).
62. *Id.* at 293.
63. *Id.* at 289.
64. *Id.* at 293.
65. *Id.*
66. *See* National Foreign Trade Council v. Natsios, 181 F.3d 38, 49 (1st Cir. 1999).
67. *Id.*
68. *Id.* at 45.
69. *Id.*
70. Natsios v. National Foreign Trade Council, 528 U.S. 1018 (1999).
71. Crosby v. National Foreign Trade Council, 530 U.S. 363 (2000).
72. *Id.* at 374 n.8 (citations omitted).

As the Supreme Court declined to rule on the dormant Commerce Clause issue, the remainder of this Note will focus exclusively on the portion of the First Circuits' decision in *Natsios* dealing with the Commerce Clause.

C. *The First Circuit's Holding in* Natsios

The First Circuit held that the Massachusetts law violated the Foreign Commerce Clause because it facially discriminated against foreign commerce, interfered with the federal government's ability to speak with one voice, and attempted to regulate conduct beyond its borders.[73] Furthermore, the First Circuit reasoned it was unlikely that the market participant exception applies to the Foreign Commerce Clause, and, even if it did, the court concluded that Massachusetts was not acting as a market participant.[74]

The First Circuit began its analysis by detailing the basis for the "dormant" Foreign Commerce Clause:

> [The] Commerce Clause grants Congress the power "to regulate Commerce with Foreign nations, and among the several States." U.S. Const. art. 1, § 8, cl. 3. It has long been understood, as well to provide "protection from state legislation inimical to the national commerce [even] where Congress has not acted."[75]

The First Circuit then relied on a 1992 Supreme Court opinion and ruled that "[a]bsent a compelling justification . . . a State may not advance its legitimate goals by means that facially discriminate against foreign commerce."[76]

In holding that the law violated the Foreign Commerce Clause because it facially discriminated against foreign commerce, the First Circuit rejected Massachusetts' argument that the law did not distinguish between foreign and domestic companies.[77] The court stressed that a "law need not be designed to further local economic

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73. National Foreign Trade Council v. Natsios, 181 F.3d 38, 66 (1st Cir. 1999).

74. *Id.* at 62, 65.

75. *Id.* at 61-62 (1st Cir. 1999) (quoting Barclays Bank PLC v. Franchise Tax Board Of California, 512 U.S. at 310 (quoting Southern Pac. Co. v. Arizona ex rel. Sullivan, 325 U.S. 761, 769 (1945) (alterations in original))).

76. *Natsios*, 181 F.3d at 66 (quoting Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue and Fin., 505 U.S. 71, 81 (1992)).

77. *Natsios*, 181 F.3d at 67. Massachusetts relied on *Oregon Waste Sys. v. Department of Envtl. Quality*, 511 U.S. 93, 98 (1994) and *Kraft Gen. Foods v. Iowa Dep't of Revenue*, 505 U.S. 71, 82 (1992) to make this argument. Massachusetts argued that the holdings in these cases require "that the law must distinguish between foreign and domestic producers in order to be held facially invalid." *Natsios*, 181 F.3d at 67. It also argued that the crucial factor in determining whether a law discriminates is not whether the law singles out a particular foreign state, but rather whether it discriminates "in favor of in-state businesses." *Id.*

interest in order to run afoul of the Commerce Clause."[78]

Relying on *Kraft Foods v. Iowa Department of Revenue and Finances*,[79] the First Circuit also explicitly rejected the argument that "local favoritism is crucial to a finding that a law is facially discriminatory."[80] Further, the court ruled that "state laws that are designed to limit trade with a specific foreign nation are precisely one type of law that the Foreign Commerce Clause is designed to prevent."[81] The court stressed that this rule was especially applicable to the Massachusetts law because "the law has clearly more than just foreign resonances . . . a chief goal of the Massachusetts law is to affect business decisions pertaining to a foreign nation."[82] This ruling was based on the assumption that "[w]hen the Constitution speaks of foreign commerce, it is not referring only to attempts to regulate the conduct of foreign companies; it is also referring to attempts to restrict the actions of American companies overseas."[83]

The court articulated that the second reason the law violated the Foreign Commerce Clause was because it interfered with the ability of the "federal government to speak with one voice."[84] Judge Lynch, speaking for the First Circuit, made certain to distinguish this line of reasoning from a similar analysis the court used when holding that the law violated the foreign affairs power:

> Independent of any claim under [the foreign affairs power], the Supreme Court decisions in *Japan Line* and *Container Corp.* make clear that a state law can violate the dormant Foreign Commerce Clause by impeding the federal government's ability to "speak with one voice" in Foreign affairs, because such state action harms "federal uniformity in an area where federal uniformity is essential."[85]

Thus, the First Circuit rejected Massachusetts' argument that

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78. *Id.*.

79. 505 U.S. 71 (1992).

80. *Id.* The *Natsios* court was relying on the *Kraft* Court's statement that it was "not persuaded . . . that such favoritism is an essential element of a violation of the Foreign Commerce Clause. . . . As the absence of local benefit does not eliminate the international implications of the discrimination, it cannot exempt such discrimination from Commerce Clause prohibitions." *Kraft*, 505 U.S. at 79.

81. *Natsios*, 181 F.3d at 67 (relying on Container Corp. v. Franchise Tax Bd., 463 U.S. 159, 194 (1983) and Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434, 448-49 (1979)).

82. *Natsios*, 181 F.3d at 68.

83. *Id.* In making this assumption, the court reasoned that "[l]ong standing Supreme Court Precedent indicates that the Framers were concerned with 'discrimination favorable or adverse to commerce with particular foreign nations [under] state laws.'" *Id.* (citing Cooley v. Board of Wardens, 53 U.S. 299, 317 (1851)).

84. *Id.*

85. *Id.* (citing *Japan Line*, 441 U.S. at 448-49; *Container Corp.*, 463 U.S. at 193).

the "one voice" test was no longer valid.[86]

Finally, the court ruled that Massachusetts was unconstitutionally attempting to regulate conduct beyond its borders.[87] The court analogized domestic dormant Commerce Clause cases to come to this conclusion.[88] It held that:

> Massachusetts may not regulate conduct wholly beyond its borders. Yet the Massachusetts Burma Law–by conditioning state procurement decisions on conduct that occurs in Burma–does just that. . . . The "critical inquiry" here is "whether the practical effect of the regulation is to control conduct beyond the boundaries of the State." Because we find that the Massachusetts Burma Law has such an effect, and is not otherwise shielded by the market participant exception, we find that the law violates the Foreign Commerce Clause.[89]

After the court determined that the law discriminated on its face in violation of the Foreign Commerce Clause, the court acknowledged that the Massachusetts law could still be found legitimate if it advanced "a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives."[90] The court determined, however, that Massachusetts had not attempted to demonstrate such a purpose.[91]

The court also vigorously rejected Massachusetts' argument that the market participant exception should apply.[92] Again relying on domestic dormant Commerce Clause cases, the court reasoned that because this case did not involve "a discrete activity focused on a single industry," the market participant exception was inapplicable.[93] It also concluded that Massachusetts' creation of the selective

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86. *Id.*

87. *Id.* at 69.

88. The court relied on several cases in its analysis, including *BMW of North America, Inc. v. Gore*, 517 U.S. 559, 571-72 (1996) (holding that "one State's power to impose burdens on the interstate market is not only subordinate to the federal power over interstate commerce but is also contained by the need to respect the interests of the other States . . . it follows from . . . principles of state sovereignty and comity that a State may not impose economic sanctions on violator of its laws with the intent of changing. . .lawful conduct in other states.").

89. *Natsios*, 181 F.3d at 69-70 (quoting Healy v. Beer Institute, 491 U.S. 324, 336 (1989)).

90. *Id.* at 70 (quoting New Energy Co. v. Limbach, 486 U.S. 269, 278 (1988)).

91. *Id.* at 70-71. The court suggested that Massachusetts could have made an argument that "expression of moral outrage about feign human rights concerns" constitutes valid local purpose. It was then was quick to reject this argument as well.

92. *Id.* at 62. The court held that "in enacting the Massachusetts Burma Law the Commonwealth has crossed over the line from market participant to market regulator." *Id.* at 63.

93. *Id.* at 63. The court distinguished this case from *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980) and *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976), two cases where the Supreme Court held that the exception applied.

purchasing list precluded the application of the exception because the list created "a mechanism to monitor the ongoing actions of private actors,"[94] and thus imposed restrictions on markets other than the market for state procurement contracts.[95] The court went on to suggest that the market participant exception should not apply to Foreign Commerce Clause cases in general.[96]

The market participant exception and the appropriateness of its application to the facts of this case will be discussed at length in the proceeding portion of this Note.

III. ANALYSIS

A. *Background and Assumptions Underlying the Foreign Commerce Clause*

Before determining whether the market participant rule should have been applied in *Natsios*, it is essential to understand the purpose behind the Commerce Clause and the justifications behind the market participant exception. The Commerce Clause provides that "Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States. . . ."[97] Although the language of the Commerce Clause merely grants power to Congress and does not literally restrict state action, the courts have recognized that it includes a "negative implication" that limits the authority of states to regulate commerce. While the courts traditionally apply this negative implication in the context of domestic interstate commerce, the courts have yet to establish the negative implication's scope in the context of foreign commerce.

B. *The Dormant Commerce Clause's Market Participant Exception*

Courts have, however, not left unchecked the negative implication that arises from the dormant Commerce Clause. Rather, in order to limit the scope of the dormant Commerce Clause, the courts have adopted a doctrine commonly referred to as the "market

94. The court held that this factor made the case analogous to *South-Central Timber Dev., Inc. v. Wunnicke*, 467 U.S. 82, 99 (1984).

95. *Natsios*, 181 F.3d at 63. The court was not clear on exactly what these "other" markets were, or how the Massachusetts law affected these markets.

96. *Id.* at 65. The court argued that, at the very least, it needed to be applied at a much higher level of scrutiny. To support its argument that the exception should not apply to the Foreign Commerce Clause, the court looked to *South-Central Timber*, 467 U.S. at 96, *Reeves, Inc. v. Stake*, 447 U.S. 429, 437 n.9 (1980), and *Japan Line*, 441 U.S. at 488. However, as the First Circuit admitted, no court has expressly ruled on the issue.

97. U.S. CONST. art. I, § 8, cl. 3.

participant exception." The Supreme Court first applied the market participant exception in *Hughes v. Alexandria Scrap Corp.*,[98] stating that "[n]othing in the purposes animating the Commerce Clause prohibits a State in the absence of congressional action, from participating in the market and exercising the right to favor its own citizens."[99] Later, in *Reeves Inc. v. Stake*, the Court again applied the market participant exception, holding that South Dakota acted as a market participant by following its policy of confining the sale of cement to state residents during a cement shortage.[100]

In market participant exception cases following *Alexandria Scrap* and *Reeves*, the Supreme Court has applied the doctrine inconsistently.[101] First, the market participant rule is not necessarily applied in every situation in which a state merely appears to be acting as a buyer or seller choosing a trading partner.[102] The Court, instead, has left itself open to either recognizing an exception to the general rule or characterizing the state as a market regulator not withstanding its superficial appearance as market participant.[103] Second, when applying the rule, Supreme Court Justices disagree on when and under what circumstances the rule should be applied.[104]

Thus, in order to understand how the rule should be more consistently applied, it is essential to examine the underlying justifications of the market participant exception. In an article that closely examines the market participant rule, Professor Dan T. Coenen outlines five key justifications underling the market participant exception. These include (1) fairness, (2) a need to avoid interference with state autonomy as consistent with federalism values, (3) a decreased risk of dangers to Commerce Clause values, (4) formal considerations emanating from constitutional text and history, and (5) institutional considerations.[105]

The first justification, fairness, rests on the fundamental distinction between state regulation or taxation and state trading in the market place:

> When a state government regulates or taxes, it turns over

98. 426 U.S. 794 (1976).

99. Hughes v. Alexandria Scrap Corp., 426 U.S. 794, 810 (1976).

100. *Reeves*, 447 U.S. at 429.

101. *See* Coenen, *supra* note 14, at 405.

102. *Id.*

103. *Id.* (citing South-Central Timber Dev., Inc. v. Wunnicke, 467 U.S. 82, 93-99 (1984); Wisconsin Dept. of Indus., Labor & Human Relations v. Gould, Inc., 475 U.S. 282, 289 (1986); New Orleans S.S. Assoc. v. Plaquemines Port, Harbor & Terminal Dist., 874 F.2d 1018, 1021 (5th Cir. 1989); Transport Limousine v. Port Auth., 571 F. Supp. 576, 581 (E.D.N.Y. 1983)).

104. Coenen, *supra* note 14, at 405.

105. *Id.* at 420.

> nothing that belongs to it; rather, it compels private action through the exercise of raw governmental power. In contrast, when a state government buys or sells, it is controlling and distributing its own resources. . . . [I]t seems sensible that when a state government distributes state resources, it may–on behalf of all its citizens–pick and choose among the proper recipients. An essential feature of having property is, after all, the right to exclude others.[106]

Therefore, under this justification of fairness, a state should be allowed to choose where and how it will spend its own money, simply because, as a property owner, it has the right to exclude others, and a state should not be precluded from exercising this right simply because a state is a group of property owners that have banded together rather than a single individual property owner standing alone.

The second justification to the market participant rule arises from underlying notions of federalism.[107] Because a state's resources "are the state's 'own' in a way that the state's regulatory powers are not," restricting a state's use of its own tangible resources is a greater "intrusion of state autonomy" than to "cabin its otherwise limitless power to coerce through government fiat."[108] Thus, the Commerce Clause "commands a closer scrutiny of state regulatory programs than of state marketplace programs."[109] Because this justification involves the state's sovereignty vis-à-vis the national government, it can be consistently applied to both the dormant Commerce Clause and the Foreign Commerce Clause when the primary concern is whether the state is overstepping its regulatory framework.

The third justification for the market participant exception is that the negative impacts resulting from permitting resident preferences in the distribution of state resources are minimal. One reason that these market participant type preferences are less threatening to "the underlying Commerce Clause goal of free trade in a unified nation"[110] than preferential regulatory or taxing programs is that when a state chooses to respond to political rather than economic concerns, it is expensive for the state, especially when the state rejects a lower priced good or service for purely political reasons. Because these types of measures have high costs, they are less likely to proliferate than measures that bear no such cost to the state.[111] Thus,

106. *Id.* at 422.
107. *Id.* at 426.
108. *Id.* at 427.
109. *Id.* at 427.
110. *Id.* at 430.
111. *Id.* at 432-33.

when a selective purchasing law is implemented at the direct expense of the state, the likelihood for widespread effects on free trade within either a national or world economy will be minimal because the high cost of such selective purchasing laws will impose a chilling effect.

The fourth justification involves textual and historical considerations associated with the market participant exception.[112] Because the text of the Commerce Clause grants Congress the power to "regulate" interstate commerce, it follows that the scope of the clause's negative implication must also be limited to activities that "regulate."[113] Therefore, under a logically construed dormant Commerce Clause theory, a state is merely prohibited from "regulating" commerce in certain respects. Although the term "regulate" is not defined within the Commerce Clause, it is unlikely that an ordinary person would consider a state acting as a purchaser to be "regulating."[114] This notion is further supported by the historical perception that traders in the market are ordinarily free to deal with whomever they wish.[115] A choice not to deal with certain entities is not traditionally seen as a regulation, but merely a business choice, even when the choice is based on moral rather than economic considerations.

Finally, certain institutional considerations justify the market participant rule. One of these considerations is that Congress remains capable of protecting national interests in the realm of commerce, even if the courts do not.[116] Accordingly, if Congress decides that it would harm national interests to allow states to pass such selective purchasing laws, it is entirely free to pass legislation prohibiting such laws.

Thus, after examination of both formal and institutional considerations, it is reasonable to conclude that these justifications are not unique to the domestic Commerce Clause. Rather, they apply to the language and the nature of the Commerce Clause itself, and therefore should receive equal weight under either a foreign or domestic analysis.

1. Application of the Market Participant Exception to the Foreign Commerce Clause

In its market participant analysis, the First Circuit glossed over

112. *Id.* at 436.
113. *Id.* at 435.
114. *Id.* at 435.
115. *Id.* at 436.
116. *Id.* at 439.

the fundamental purpose of the Foreign Commerce Clause and the justifications underlying the market participant exception when it concluded that it is unlikely that the market participant exception applies to the Foreign Commerce Clause.[117] In addressing the purpose of the Foreign Commerce Clause, the court stated, "[l]ike the dormant domestic Commerce Clause . . . [the Foreign Commerce Clause] restricts protectionist policies."[118] The court went on to suggest that a second purpose behind the Foreign Commerce Clause is to restrain the states from excessive interference in foreign affairs.[119] Not only did the court fail to cite authority when making this assertion, it also failed to examine the justifications behind the market participant exception. Finally, the court failed to provide any analysis as to why these justifications would not be applicable to the Foreign Commerce Clause.

There are, however, two reasons that the justifications discussed in the analysis above can be applied to justify the market participant exception in either a foreign or domestic context. First, regardless of whether the commerce in question is foreign or domestic, the fundamental purpose behind the Commerce Clause is, as the First Circuit in *Natsios* admitted, to prevent protectionism.[120] Second, upon closer examination, the various justifications for the market participant exception primarily focus on the relationship between the states and the federal government.[121] Therefore, the justifications for the market participant exception are applicable in the context of both foreign and domestic commerce.

2. In Passing its Law, Massachusetts Was Acting as a Market Participant

Even though the First Circuit in *Natsios* was reluctant to apply the market participation exception in a Foreign Commerce Clause context, it took the opportunity to hold that Massachusetts was not acting as a market participant when it passed the Massachusetts Burma Law.[122] In reaching its conclusion that Massachusetts was not a market participant, the court relied heavily on the Supreme Court's holding in *Camps Newfound/Owatonna v. Town of Harrison*.[123]

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117. National Foreign Trade Council v. Natsios, 181 F.3d 38, 65 (1st Cir. 1999).

118. *Id.* at 66 (citing Houlton Citizens' Coalition v. Town of Houlton, 175 F.3d 178 (1999)).

119. *Id.*

120. *Id.* at 66.

121. *See generally* Coenen, *supra* note 14.

122. *Natsios*, 181 F.3d at 62.

123. *Id.* at 63.

Camps involved a Maine statute that provided certain nonprofit entities with an exemption from real estate and personal property taxes, so long as the institutions' activities were conducted principally for the benefit of persons living in the state.[124] The Supreme Court in *Camps* held that the market participant exception did not apply to the tax exemption because the tax exemption could not be characterized as a "proprietary activity."[125] The Court stated that the inquiry was "whether the 'challenged [tax] program constituted direct state participation in the market,'" and held that it did not.[126] The Court's holding in *Camps* was, therefore, narrow in that it pertained to taxing schemes. Because the narrow *Camps* holding failed to provide a basis to invalidate the Massachusetts law, which involved direct purchasing activities rather than taxation, the First Circuit instead resorted to the following dicta to support its conclusion that Massachusetts was not acting as a market participant:

> More recently, in *Camps Newfound/Owatonna* . . . [t]he Court said that the market participant exception is a narrow one, noting that *Reeves* and *Alexandria Scrap* both involved "a discrete activity focused on a *single industry*. . . ." The court warned against an expansion of the market participant exception that "would swallow the rule against discriminatory tax schemes."[127]

The First Circuit, however, incorrectly relied on this portion of the *Camps* opinion as a primary basis for refusing to apply the market participant exception. First, the *Camps* Court did not apply this reasoning until after it held that tax exemptions are not the type of activities that fall into the market participant exception, so it was not essential to the holding. Second, a closer examination of *Reeves* and *Alexandria Scrap* reveals that the Court, in deciding these cases, did not, as the *Camps* Court arguably suggests, place emphasis on the relative scope of the market in its application of the market participant exception.[128]

In *Reeves*, due to a cement shortage, the State of South Dakota

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124. *Camps*, 520 U.S. at 569. Institutions that did not meet this requirement could generally receive a more limited benefit under the statute.

125. Thus, when acting in the role of a market participant, a government should be able to choose its business partners, regardless of its reasons for doing so, and regardless of whether the business partners are foreign or domestic.

126. *Camps*, 520 U.S. at 593 (quoting White v. Massachusetts Council of Constr. Employers, Inc., 460 U.S. 204, 208 (1993)).

127. *Natsios*, 181 F.3d at 638 (quoting *Camps*, 520 U.S. at 594) (emphasis added).

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

reaffirmed its policy to limit the sale of cement made by the state-owned plant to residents of the state.[129] A Wyoming ready-mix concrete distributor that had relied on the cement produced by South Dakota was denied supplies and brought suit, claiming a violation of the dormant Commerce Clause.[130] In holding that the state action fit into the market participant exception, the Supreme Court considered only the analysis provide by *Alexandria Scrap*:

> The basic distinction drawn in *Alexandria Scrap* between States as market participants and States as market regulators makes good sense and sound law. As that case explains, the Commerce Clause responds principally to state taxes and regulatory measures impeding free private trade in the national marketplace. There is no indication of a constitutional plan to limit the ability of the States themselves to operate freely in the free market. The precedents comport with this distinction.[131]

The *Reeves* Court, however, was not clear on how it applied this doctrine to the facts of the case. It merely stated that "South Dakota, as a seller of cement, unquestionably fits the 'market participant' label more comfortably than a State acting to subsidize local scrap processors."[132] It concluded, "the general rule of *Alexandria Scrap* plainly applies here."[133] Thus, the *Reeves* Court gave no indication that it relied on the fact that only a single market was affected. It is just as plausible to assert that the Court relied on the fact that the State was acting as a seller of goods in a market.

Alexandria Scrap does not help to clarify this point either, as it does not specify reliance on the fact that there was only a single market involved. In *Alexandria Scrap*, the State of Maryland enacted legislation that allowed scrap metal processors, located both in and outside the state, to collect a "bounty" for every junk car with a Maryland title converted into scrap metal.[134] The purpose of this program was to remove abandoned automobiles from the state's roadways and junkyards.[135] Five years after the original legislation was passed, it was amended to require documentation for cars over eight years old (hulks).[136] This amendment had the effect of imposing more stringent documentation requirements on out-of-state

129. *Reeves*, 447 U.S. at 432.
130. *Id.* at 433.
131. *Id.* at 436-37 (citations omitted).
132. *Id.* at 440.
133. *Id.* at 440.
134. Hughes v. Alexandria Scrap Corp., 426 U.S. 794, 797 (1976).
135. *Id.* at 796.
136. *Id.* at 798-99.

processors.[137] The Court did not refer to the scope of the market when it determined that the state action fell into the market participant exception.[138] It merely held that:

> Maryland has not sought to prohibit the flow of hulks, or to regulate the conditions under which it may occur. Instead, it has entered into the market itself to bid up their price . . . as a purchaser, in effect, of a potential article of interstate commerce, [and has restricted] its trade to its own citizens or businesses within the State.[139]

Thus, this holding does not suggest that the Court considered Maryland's action "a discrete activity focused on a single industry" when it determined that the market participant exception applied.[140]

The *Camps* Court also cited to *White* when it suggested that the Court must construe the market participant exception narrowly.[141] Although the *White* Court did recognize that there were limits to the market participant exception, the language relied on by the *Camps* Court merely states:

> We find it unnecessary in this case to define [the limits on a state or local government's ability to impose restrictions that reach beyond the immediate parties with which the government transacts business] with precision, except to say that we think the Commerce Clause does not require the city to stop at the boundary of formal privity of contract. In this case, the Mayor's executive order covers a discrete, identifiable class of economic activity in which the city is a major participant. Everyone affected by the order is, in a substantial if informal sense, "working for the city." Wherever the limits of the market participation exception may lie, we conclude that the executive order in this case falls well within the scope of *Alexandria Scrap* and *Reeves*.[142]

If anything, when viewed in light of the facts and holding in

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137. *Id.* at 803 n.13.

138. *Id.* at 803, 806.

139. Reeves, Inc. v. State, 447 U.S. 429, 435 (1980) (citing *Hughes*, 426 U.S. at 806, 808). According to the *Reeves* Court, "the [*Alexandria Scrap*] Court invoked this rationale after explicitly reiterating the District Court's finding that the Maryland program imposed 'substantial burdens upon the free flow of interstate commerce.'" *Alexandria Scrap*, 426 U.S. at 804. Moreover, the Court was willing to accept the Virginia processor's characterization of the Maryland program as "reducing in some manner the flow of goods in interstate commerce." *Reeves*, 447 U.S. at 435 n.7.

140. *See Camps*, 520 U.S. at 594.

141. *Id.* (citing White v. Massachusetts Council of Construction Employers, Inc., 460 U.S. 204 (1983)).

142. *White*, 460 U.S. at 211 n.7.

White, this passage, contained in a footnote, supports Massachusetts' position that the Burma Law fell under the market participant exception because everyone contracting with the state is essentially working for the state. Although it did have some downstream effects, the Massachusetts Burma Law, like the law at issue in *White*, only required contractors not to do business with Burma before or during the time that they contracted with the state. After performing the contract, they were free to do business with Burma. Additionally, the law at issue in *White* can be considered even more restrictive than the Massachusetts Burma Law because the latter did not categorically exclude all businesses doing business with Burma; rather, it merely disadvantaged them by requiring them to offer a lower bid.

Because the dicta in *Camps* suggests that the market participant exception should be more readily applied to those cases involving "discrete activity focused on a single industry,"[143] the court in *Natsios* should not have relied on it to conclude that the market participant exception did not apply.[144] Rather, the First Circuit should have assessed "whether the challenged 'program constituted direct state participation in the market.'"[145] To do so properly, it would have been important to determine whether Massachusetts was acting as a private individual would in the market place. The *Reeves* court provided helpful guidelines for such an analysis:

> *"[like] private individuals and businesses*, the Government enjoys the unrestricted power to produce its own supplies, to determine those with whom it will deal, and to fix the terms and conditions upon which it will make needed purchases." While acknowledging that there may be limits on this sweepingly phrased principle, we cannot ignore the similarities of private businesses and public entities when they function in the marketplace.[146]

Massachusetts, in passing the Burma Law, appears to fit neatly into the category of private individual, as it used the Burma Law as a mechanism for determining with whom it would deal, and under what terms and conditions. Therefore, because of its functional role in the market place, Massachusetts was acting as a market participant when it passed the Burma Law.

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143. *Camps*, 520 U.S. at 594.

144. *Natsios*, 181 F.3d at 63.

145. *Reeves*, 447 U.S. at 435 n.7 (quoting Justice Powell's dissent at 451). This was the question posed in *Alexandria Scrap* and *Reeves*.

146. *Reeves*, 447 U.S. at 438 n.12 (emphasis in original) (quoting *Perkins* v. *Lukens Steel Co.*, 310 U.S. 113, 127 (1940)).

IV. CONCLUSION

Although the First Circuit held that the Massachusetts Burma Law was unconstitutional for many reasons, both the First Circuit and the Supreme Court should have recognized that the market participant exception shielded the state from violating the Foreign Commerce Clause by passing the law. By failing to consider the justifications behind the rule, the First Circuit overly limited the market participant exception. Under its interpretation, states are wrongfully precluded from choosing their foreign trading partners. Not only are states stripped of their choice to do business with foreign countries, but they are also precluded from imposing many of their own terms on these business transactions. This outcome could prove to be troublesome given the increasing globalization of domestic economics and the continuing removal of trade barriers, leaving a plethora of tough choices for both states and individuals who wish to use consumer choice as a mechanism to foster human rights and environmental protection.

The Massachusetts Burma Law provided the state with a feasible framework for dealing with these tough consumer choices, and it was a prime candidate for the market participant exception. Although it appears that the circumstances surrounding the Massachusetts Burma Law, including the federal legislation and the list of actors involved, placed the it on a path destined toward failure, a more favorable holding by the courts regarding the market participant exception would have allowed the law to be used as a model for other local governments wishing to exercise their consumer choice in a manner consistent with the greater good.