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TAXATION, REGULATION, AND
CONFISCATION

By RICHARD A. EPSTEIN*

I. GENERAL THEORY

The recent studies on regulation have underscored an emerging truth in the study of law and economics. The traditional modes of classification and analysis no longer suffice to organize the study of legal institutions and legal rules. In a former day it was quite fashionable to place public and private law into rigid, separate compartments, each governed by its own set of rules. Within the area of private law, it was possible to draw sharp and clear lines between contract, tort, property and restitution. Within public law, it was fashionable to study the various techniques of social control in isolation from one another. Taxation could be placed in one box, regulation of wages and prices in another, and licensure of all forms of activities in still a third. These traditional typologies do identify the relevant techniques, but they must not be allowed to conceal the larger structure of government action. The key point is a simple one: all of the various means of social control, public and private, can be applied, either alone or in combination, to any designated set of activities. Each remedy is, or may be, a close substitute for each of the others, such that the strength and effectiveness of the one must be evaluated in its relationship to all the others. In one sense this observation serves as a charter of emancipation for the policy analyst, as it makes explicit the rich array of tools available to encourage or discourage, mandate or prohibit, various forms of social activity, all without apparent limitation. A set of original endowments may be turned at will to maximize some defined set of outputs in a world in which the policy maker is king.

Into this picture of uncontested hegemony I should like to inject a note of doubt. It must be asked by what warrant, by what title, does the public policy analyst proceed on the implicit assumption that all entitlements lie within the public domain? At the very least the question deserves some sort of an answer because of the way in which the study of law and economics—even that of a conservative stripe—cuts against the ideals of limited government, individual liberty and private property, which, especially in the American context, have deep and powerful roots of their own. At the root of this conception is the persistent fear of abuse of power—that persons, clothed in official garments, will convert a limited delegated authority into an absolute source of power over others. This fear is so pervasive that it

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1 See, e.g., Madison, The Federalist (New York: Holt and Co., 1898) at 54 (No.10).
colours our view of social institutions. Government is viewed not as an inherent kind of good, but as a necessary evil required to ward off the greater evils of aggression and despoliation by self-interested individuals. The task of constitutional theory, then, is to organize political institutions in ways to prevent the state from becoming an organized menace greater than the individual misdeeds that it is designed to control.

To achieve this ideal of limited government, the powers of government can be parcelled out in different layers, as in a federal system. Within each layer of government, the principle of the separation of powers can place the premium on caution instead of on speed. Complicated voting rules and procedures can limit further the ability of a transient majority to impose its will upon the population as a whole. The effective constraints upon the power of government, however, need not be only structural and procedural. There is still the substantive question: what ends should government serve? Here it does seem clear, to one not nourished upon the British tradition of parliamentary supremacy, that some explicit individual safeguards against government and the will of the majority should be entrenched in a bill of rights. At the same time it seems equally clear that the individual rights so entrenched should not be so vast and extensive as to paralyze all government action.

How then do taxation and regulation fit into this sceptical view of government powers? Here we can start with the received wisdom that each is a close substitute for the other, and note that the differences between them all go to matters of detail and technique, rather than to basic principle. Now push that equivalence one step further. Regulation and taxation both may be used as instruments of confiscation, because both are the equivalent of the (partial) taking of private property. To understand this, it is necessary only to accept two propositions. The first is that the loss of any right in property is like a loss of property itself. To deny that proposition is to say that the state can take sticks in the bundle of rights one by one without compensation, when compensation would be required if the taking of the entire bundle were compressed into a single step. Here the central point remains obvious. It is insufficient to control the obvious abuses of outright confiscation if its close substitutes are left unregulated and uncontrolled. There is no sense to a system which allows the government, under the guise of regulation, to take interests in real estate—for example covenants or easements—worth ninety percent of the land itself without paying a dime, when the government is required to pay full value for the land, if taken outright. In effect, the distinction between complete and partial losses sets up a sharp discontinuity in the costs to government of the different modes of acquiring interests in real property. Under the banner of regulation it can acquire, without cost to itself, a limited interest in property worth ninety percent of the fee. In the alterna-

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3 A taking by government in the exercise of its power of eminent domain must be accompanied by just compensation: *U.S. Const.* amend. V. See infra note 9 and accompanying text.
tive it can acquire the full fee for its market value. As it sees matters, therefore, the full cost of the property is embedded in the acquisition of its last tenth. It is no wonder then that the government will not purchase the fee when it can take the limited interest.

The second proposition is that the taking from many individuals at the same time does not insulate the state from the charge of a taking any more than it does a private individual. Thus murder is a wrong and so too is genocide. The thief is not purged because he has taken from all the members of a group instead of only one, and the unfortunate private defendant who runs down a busload of children cannot escape his liability because he has damaged many persons instead of one. The progression from the single to the many on the question of what constitutes a taking of property—in whole or in part—is itself a matter of simple summation. There is no subtle interaction of the parts which allow takings from many to be viewed as something else solely because they are directed to a large number of individuals at any given point in time. Efforts have been made to avoid that conclusion, and thereby to restrict the reach of the eminent domain clause in American constitutional litigation. It has been said for example that the power of eminent domain is one thing, and the power of taxation is quite another; and so too the police power has been said to be one thing, the eminent domain power quite another. These rigid schemes of classification are designed to blunt the compensation requirement of the eminent domain principle and historically, with taxation and regulation, they have largely succeeded to that end. On intellectual grounds, however, the strategy simply will not work. An eminent domain provision in any scheme of constitutional government is not a grant of additional power to government. Instead it places a limitation upon the powers of government that are already in place, including both general powers of taxation and regulation. In both cases, that limitation upon government will be idle if by persuasive redefinition the state can defeat the obligation to compensate that it otherwise should incur. Taxes and regulation are forms of taking, to be examined under principles applicable to all other takings.

To say this much, however, is not to insist upon a strict equivalence between taxation, regulation and confiscation. Indeed, to equate taxation and regulation with theft is to condemn all government at the outset, as there is none that could function without resort to these powers. How can we avoid this extreme result, steer a middle course, and identify those forms of taxation and regulation that should survive, and those that should be condemned?

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6 The term confiscation is not used in the sense that is appropriate when, for example, government officials confiscate stolen property or smuggled goods. Those cases are best understood as instances in which the taking, although called confiscation, is justified by the police power given the prior wrong of the individual against whom the power is directed. That form of justification is, however, far removed from the concerns here.
To approach this question it is best to consider the simplest form of the taking of property, say the taking of land for use as a post office, and ask what differentiates it from the illicit confiscation of that same land. That some difference exists seems clear enough; we all understand that killing and murder, although related, are very different affairs. While killing may be justified, for example, in self-defense, calling a particular killing murder means that the possibility of justification in the particular case has been excluded. So too with the analogous relationship between the taking of property and the theft of property; the first admits the possibility of justification that the second precludes. With this much said, the relationship between taking and confiscation can be captured by the following proposition: the taking of private property is *prima facie* confiscation. So too its close substitutes, the partial takings by way of regulation and taxation. But to treat the taking as only a *prima facie* wrong is to admit the possibility of justification.

With government it seems proper to recognize two separate justifications, one of which it shares with the private individual who wishes to acquit himself of the charge of theft, and one of which is unique to its special status as the monopolist of force within the jurisdiction. The first of these generally goes in public law discussions under the name of the police power and can be defined quite simply as the power of the state to prevent the commission of wrongs—for example the taking of property, the use of force or fraud—by one individual against another. The principles that govern taxes and regulations directed towards this end are difficult enough in their own right, and I will not dwell upon them here, except to note that there is no principled way that the exception, so useful in nuisance control matters, can account for the comprehensive revenue measures and the major forms of social regulation—price controls and the like—in issue here. The crux of the matter therefore lies in the second justification: that of making compensation, explicit or implicit, for a taking for a public purpose brought about against the will of the owner.

In most cases the easiest way to tender compensation is with money, but there is no strict requirement for its use, even if it is invariably used with, say, the taking of an isolated parcel of land. More importantly for these purposes, this cash remedy will not work in every case. Taxes and regulation are partial takings, either from all individuals or a very large group of them. There is at this point a circular and self-defeating quality about any insistence upon explicit compensation. The money raised in taxes must now be returned to the very individuals from whom it was collected. A regulation would require the imposition of additional taxes to compensate the regulated parties for their losses, which in turn makes the taxes levied themselves uncompensated takings. Therefore, with co-ordinated takings from a large number of individuals, explicit compensation can no longer be the norm, but the rare

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8 The classic discussion is contained in Freund, *The Police Power* (Chicago: Callaghan & Co., 1904).
exception. What must be reckoned as the compensation for the property taken are the benefits received from the government operations, be it in the provision of roads, of police protection, or in the administration of justice, or whatever.

In a well-ordered state there is some reason to believe that the benefits derived from taxation and regulation will exceed the correlative costs. But it is one thing to make the assertion and quite another to demonstrate its truth. The nub of the difficulty is that any shift from explicit to implicit compensation makes it quite difficult to calculate the size of the benefits received, even if (itself a somewhat doubtful assumption) the costs in question can themselves be calculated precisely. The question is whether these difficulties make it necessary to retreat to one of two extremes, both of which seem quite untenable. Either no taxation or regulation is allowed, or all taxation and regulation is allowed. Either government ends, or the constraints imposed upon it lie in the political process, where the unfairness found in regulation or taxation is to be beaten back or endured. Follow the line and the policy analyst has his domain at last, at least that portion of it—comprehensive control—that he covets most.

In general, this second alternative has been embraced, even in the United States with its strong constitutional tradition and its explicit eminent domain provision. “[N]or shall private property be taken for public use, without just compensation.” While it is possible to find grudging concessions by American judges that certain forms of regulation and taxation can go “too far”, the more basic truth is that the supposed limits are never reached no matter what the form of government exaction.

The only way to blunt this massive rejection of limited government on economic matters is to find some intermediate position that:

(a) allows limited supervision of the powers to tax and regulate,
(b) escapes the burdens of direct measurement, and
(c) blunts the greatest abuses of government.

Here the central insight is contained in a principle of American eminent

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9 U.S. Const. amend. V. Note that the same argument can to some extent be made in the American context from the language of the taxing power, in U.S. Const. art. I, s. 8, cl. 1:

The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defense and general Welfare of the United States; but all Duties, Imposts, and Excises shall be uniform throughout the United States.

The references to “common”, “general”, and “uniform” all hint at the disproportionate impact test which itself has been incorporated into the eminent domain clause.
domain law, whereby the disproportionate impact of a tax or regulation functions as an indirect measure of the adequacy of compensation. Although used in some contexts, this test to date has not been applied seriously to taxation and regulation, largely because of the occupational hazard of lawyers which prevents them from taking a comprehensive approach to the various forms of social control.

The extension of the disproportionate impact principle to taxation and regulation would not be sufficient in and of itself to strike down all unfortunate forms of regulation and taxation. But the rule, even if underinclusive, does provide strong incentives to control the behaviour of the state. Within rough practical limits, the prohibition against disproportionate impact is designed to insure that no one will be able to obtain benefits that exceed costs without extending these same benefits to all other individuals who are also subject to the regulation. The rule therefore helps prevent the creation of a situation in which the proponents of a tax or regulation enjoy benefits in excess of costs while others are made to bear costs in excess of benefits. To be sure, the rule does nothing to prevent a situation in which a general tax or regulation leaves everyone in the system—be they proponents or opponents of the new regime—worse off than they were under the old: if everyone were left worse off, then the impact, while undesirable, would not be disproportionate. Nonetheless, it is doubtful that the unfortunate state of affairs created by such a law would be stable over time, in as much as it leaves all persons net losers. If all (or nearly all) persons are left worse off under the regulation or the tax, then no one would have any incentive to work for its adoption or preservation. The principle therefore exerts powerful incentives to ensure adoption of only those measures that advance collective welfare, however defined. On the other hand, it prevents the paralysis that follows from adherence to a unanimity requirement for social change, as the state power to force exchanges means that the “hold-out” person may be bought out, not for his asking price, but for some price which leaves him at least as well off as he was under the previous legal regime.

To state the general thesis in this fashion is, however, not to answer all the objections that can be raised against it. The initial set of difficulties comes at two levels. The first concerns the potential reach of the disproportionate impact test. The second concerns its consequences: when it applies, will the

12 See, e.g., Armstrong v. United States, 364 U.S. 40 at 49, 80 S.Ct. 1563 at 1569 (1960): “The Fifth Amendment's guarantee that private property shall not be taken for a public use without just compensation was designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.” See also, Louisville Bank v. Radford, 295 U.S. 555 at 602, 55 S.Ct. 854 at 869 (1935), for a similar expression of the basic sentiment. In one sense the Radford case is the more relevant one here, for in it the Supreme Court struck down on eminent domain grounds legislation that destroyed the existing liens of a very broad class of creditors against a very broad class of debtors. The special legislation involved in that case was akin to a tax because it possessed a degree of generality that was not found in Armstrong, supra, where what was in issue was a subcontractor lien on several uncompleted boats.
First, deciding whether a given tax or regulation is disproportionate will not normally be a simple affair. It is, for example, very difficult to determine in the abstract whether a head tax or a proportionate income tax is required, or whether a progressive income tax—whose possibilities for abuse are manifest—is permitted. Indeed the possible scope of the principle goes further, to reach all the protean forms of taxation that have been used by government from time immemorial to raise the revenues of the state. Special taxes upon certain commodities—for example, liquor—have long been a staple in the government arsenal. Distinctions between various forms of property—for instance, differential tax rates for commercial and residential real property—have become a standard feature of municipal taxation. Special rules for certain industries, such as insurance, or certain forms of voluntary associations, partnerships, corporations, or trusts, have always been adopted.

Yet while the attack on current practices may be extensive, this alone does not furnish any reason in principle to shrink from the general consequences of this position. At most, invalidation mandates a general simplification and unification of taxation and regulation. It does not, however, limit the level of government expenditures or taxation, or even require anything like a balanced budget. To be sure, it goes against long-standing practices in a great number of instances, but this itself only means that it is an instrument that limits the long-standing abuses of government power. Unlike most efforts at aggressive constitutional action, for example, busing, the eminent domain principle operates only as a constraint against legislative or administrative action, and not as its spur.

It may be said as well that the constraints, even if imposed, will be of no real consequence. But a single constraint upon the operation of government power, if the right one, can bite hard. To deny its force in the context is somewhat like saying that the principle of “one man, one vote” should be rejected because it still leaves government officials a certain amount of freedom to gerrymander voting districts. But although some degree of freedom is left, the area in which it operates is sharply circumscribed. In the analysis that follows, three recent special taxes are considered: those against mining companies for the benefit of black lung disease victims, the windfall profits tax, and the Montana coal severance tax. The sums of money involved in each case are so substantial, and their incidence so skewed, that it is quite unlikely that any government could pass neutral legislation governing income that had anything like the distributional consequences of these taxes. There would be no way in which to target the tax against the same persons, and the revenues so derived from indirect measures would be difficult to calculate and would in any event fall into the general pool where they could not be earmarked for any specific purpose or group. And if various

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government officials tried to strike up a deal to reintroduce the prohibited scheme “by the back door”, ample documentary and testimonial evidence would help pierce the new artifice; all abuses would not be eliminated, but many could be curtailed. The old ways of doing business could not last in the new constitutional order. In an ideal constitutional system more explicit constraints upon powers to tax and regulate might be appropriate, however difficult to formulate. But as a general matter, even the limited protection provided by the eminent domain clause is preferable to no protection at all.

Administrative matters to one side, a further challenge might be made: why is it that disproportionate impacts are regarded as improper in taxation and regulation when they are tolerated in the original acquisition, as by first possession, and in subsequent voluntary transfers of rights? Here the answer lies in the very different function of the two types of rules. The original rules of acquisition operate in an environment in which no person has vested rights in external things. Likewise a voluntary transfer of admitted rights is not a violation of the rights of others; for A to sell his house to B is not to commit a tort against a stranger, C. Under these circumstances there is simply no occasion to address the question of whether certain private acts have disproportionate impacts, for the issue of compensation to others, to which the disproportionate impact test applies, simply does not arise. Only after a widespread taking of private property—a wrong by the state—has been established does that question become relevant as an indirect measure of the levels of compensation that are required by the eminent domain principle.

But to all this it could be said that it is improper to look at the matter from such a narrow and incremental view, as the chief normative objection to the eminent domain principle itself is that the current distribution of entitlements has been obtained by improper and illicit means. What is needed, the argument continues, is not the protection of the rights now asserted, but a return of property to the persons with superior title to it. That such may be a legitimate attack on certain holdings of wealth cannot in principle be denied. The original entitlements of the various Indian tribes is one case in which the argument might well have powerful bite. Yet what is interesting about most schemes of taxation and regulation is that they are not justified by challenges to the legitimacy of the current holdings of the parties so taxed or regulated. No one in support of price controls, minimum wage laws, or various forms of special taxation is prepared to assert, let alone establish, that the original parties improperly acquired such holdings. Indeed if their acquisition had been tainted, these property possessors, not being owners, would not have been simply regulated or taxed. Instead their property would have been taken away by main force without regard to the residual interest left to the aggrieved party. In short, prior wrongful acts of any given party will justify state responses commensurate with the wrongs in question. But this will not justify any massive system of taxation or regulation that does not allege, let alone establish, such wrongful conduct.

14 See, for my views on this subject, Epstein, Possession as the Root of Title (1979), 13 Georgia L. Rev. 1221.
The last objection to the disproportionate impact test is in reality an objection to the larger requirement of compensation when the government takes private property. Quite simply, the point is that wealth redistribution is a proper function of the state, one that is precluded by a systematic adherence to the eminent domain principle. In one large class of cases the point can, I think, be easily turned aside. It is very difficult to think of an intelligible moral principle which tolerates wealth transfers from some well-to-do individuals to other persons of the same class, or, as is often the case through taxation and regulation, from the poor to the rich. In preventing, therefore, the voters in a local municipality from imposing extensive land use restrictions upon the isolated owners of undeveloped lands, the eminent domain principle works at its best by blocking (de facto, through the insistence upon payment of compensation) a set of measures that causes a capricious transfer of wealth from some individuals to others, and dissipates overall wealth by inducing expenditures of resources either to secure or to resist the passage of the regulation in question.

This first reply is, however, not decisive across the board because it does not address the efforts to redistribute wealth from rich to poor as part of a comprehensive welfare scheme. In truth, the case for such redistribution by compulsory means is far from clear, as it must be explained why poor individuals are entitled to obtain through the intervention of the state those benefits which they could not individually claim directly from the rich themselves: need alone never generates an entitlement, because it never shows which person should pay, or why. The institution of welfare may be defended on the ground that its universal acceptance points to an overwhelming social consensus in its favour, a consensus that serves as a close enough substitute to the ideal of individualized and unanimous consent demanded by a rigorous theory of individual rights. Yet this rationale itself suggests that redistribution is principled only if it satisfies at least one stringent condition. It will simply not do for the poor—by votes—to place unlimited exactions upon the rich. If it is the consent of the donors that matters in principle, then the preferences of the donees, even if registered in votes, can hardly be decisive, whether on the amounts of the coerced transfers or the conditions on which they should be made. Nor are matters made better if some rich join in the demands of the poor, especially if they contrive the passage of special taxes or regulations that fall exclusively on others in the population opposed to the general redistributive scheme. The principled limitation upon the power of the state has, however, been met and exceeded by a whole host of recent special taxes and regulations, whose disproportionate impacts are evident from the face of the legislation itself. In this paper I shall discuss four such systems of special legislation: black lung disease compensation programmes, the windfall profits tax on crude oil, special state severance taxes upon coal and the Canadian regulation of foreign investment. The first two programmes in large measure deal with redistributions from rich to poor, while the second two do not. Yet even if allowances are made in the first two cases for redistributive goals, all four schemes should be condemned in any system that respects both private property and the need for limited government.
II. APPLICATIONS

A. Black Lung Compensation Programme

The black lung disease compensation programme was enacted by the United States during the early 1970s in order to establish a special fund for the compensation of those coal mine workers disabled by black lung disease. The funds for the programme originally came in part from general revenues and in part from special charges imposed upon mines in order to make disability payments to former employees in the individual mines. To the firms so burdened, the payments in question were like a special tax on established mines. The competitive differential between old and new mines became so great, however, that Congress thereafter modified the programme to require all mining companies to contribute to the fund on the same basis, including newly established mines that had never employed any workers benefiting from the plan. In imposing the particular tax, it was conceded that there was no unsatisfied legal obligation running from the mines (old or new) to the covered workers, as all claims in tort or under workers' compensation law were properly barred, if ever valid. While there was some causal nexus (at least in the case of the old mines) between the injury to the workers and the mines, the nexus was wholly insufficient (and recognized as such) to support any form of legal responsibility whatsoever.

In dealing with the black lung disease compensation programme, the United States Supreme Court in Usery v. Turner Elkhorn Mining Co. sustained the tax on grounds that fulfilled the dreams of the policy analyst intent upon securing his widest domain. In effect, it recognized that the tax was unfair; that being retroactive it could have no incentive effects, desirable or otherwise; and that the current exposures to dangerous substances were extensively controlled by other regulatory systems. It stopped short of calling the tax a taking from one class of individuals followed by a gift to another, although that is what it was.

Let it be agreed that some redistribution by the state is permitted; it still does not follow that there should be no constraints upon the appropriate patterns of redistribution. As noted above, the ability to generate special benefits without any constitutional limitations—one half the policy analyst's dream—should only spur demand for effective limitations upon the collection of the wealth to be redistributed. No narrow segment of the rich should be singled out for special burdens, even if some narrow segment of the poor is selected for special benefits. There will be some greater effort for legislative responsibility if the funds in question must be drawn out of general revenues than if they can be taken from one narrow group of the population, whose members receive none of the moneys so collected. It is better by far that as many as possible of those in favour of the redistribution be made to pay their pro rata share, for one is apt to be somewhat less generous when the coercion

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16 428 U.S. 1, 49 L.Ed. 2d 752, 96 S.Ct. 2882 (1976).
of another comes at the price of payment by one's self. Therefore, to permit complete freedom as to both the objects of taxation and the beneficiaries of the tax is to allow a comprehensive scheme of confiscation which should not escape either constitutional condemnation (in the American system) or moral condemnation (everywhere). The grander the scheme of redistribution, the greater the need for its social control.

B. Windfall Profits Tax

The principles used to analyze the black lung disease compensation programme can be carried over in straightforward fashion to the analysis of the American windfall profits tax upon crude oil. The tax itself, when reduced to its essentials, is imposed upon the difference between the fair market value of the crude oil, and the price for which it could be sold under the previous scheme of direct controls. As regulated prices for all forms of oil were originally set quite low in the name of consumer protection, the differential between the market value and the regulated price became quite substantial after the major rise in world energy prices during the 1970s. As the tax ranges from sixty to seventy-five percent, it is evident that billions in revenue are at stake.

Standing alone, the windfall profits tax places a disproportionate burden upon one class of property—to wit, crude oil. The forbidden redistributive aspects of the tax are even more evident when two additional points are noted. First, large portions of the tax are designed to go into general trust funds, with an eye toward the improvement of transportation, the condition of the aged, and the like. There is thus no possibility of arguing that the tax is imposed in order to offset some special benefit to the oil industry. Second, the supporters of the tax note with great pride that the owners of crude oil cannot pass the tax forward to consumers.

Under existing American case law there is no effective way to challenge the tax. But taking the case on its merits, the disproportionate burdens condemn the tax. To this charge it might be answered, the legislative intention notwithstanding, that the tax is passed forward and thus falls generally upon the public at large, that benefits and burdens do match after all. Here it would be pointless for any court to attempt to assess the precise ways in which this tax...
particular tax works itself into the fabric of the economy. The real question therefore is what attitude it should take if it is serious, as it should be, about making sure that taxation is not a disguised form of confiscation—even on the generous view that allows some redistribution to the poor not financed by special taxes. In my view, the risk of error should fall squarely upon the government because it has adopted the means which make it so difficult to trace out the consequences of the taxes that it wishes to impose. How can the government object if it is required to impose the very general revenue tax—here a broadly based income tax—which it claims, in effect, to have imitated?

There is no question that the ordinary conception of ownership includes the rights to possess, use and dispose of the thing in question. Should the state demand that some oil not be sold at all, it will have taken from the original owner an incident of ownership which is valued at the difference between the value of the oil in exchange and its highest value in use to that particular owner. Where the government allows the oil to be sold, but at a regulated price below fair market value, the principle does not change, even if that which has been taken from producers is given to consumers, or, for that matter, wholly dissipated. The incident of disposition is not wholly removed, but compensation for that part of the incident which is taken must be made nonetheless. To this it might be suggested that it is odd in the extreme to speak of the taking by the government “of a part of a part”, especially when the government as such does not keep the part so taken. But there is confiscation if the government says to a landowner that it will take a half of a half of his land, just as when it says it will take a quarter thereof. And it would make no difference if it gave the land to some group of worthy individuals instead of keeping it for itself, or ruined it for cultivation. Why then should there be any difference when we speak of the right implicit in ownership to sell the oil in question? Here the market price is the only proper benchmark against which regulation or taxation should be measured because it is the only price which respects the unfettered right to dispose (to those who wish to purchase) that counts as part of the original bundle of ownership rights. The regulation is the wrong benchmark against which to measure the entitlements of the individual owner against the state. To be sure, the invalidation of the tax would lead to a contraction of all government programmes and services, including those with redistributive ends. But this counts as a strength

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10 There is a parallel argument in the tort literature from the law of negligence. Thus, where a defendant is negligent, and his negligence has destroyed some evidence that is necessary to establish the linkage between his negligence and the plaintiff’s harm, the court will shift the burden of proof to the defendant on the question that his own wrong has made more difficult to answer. The leading American case on the issue is Haft v. Lone Palm Hotel, 3 Cal. 3d 756, 478 P. 2d 465, 91 Cal. Rptr. 745 (1970). The analogous case for Canadian law is McGhee v. National Coal Bd., [1972] 3 All E.R. 1008 (H.L.).


21 That is, the amount obtained by applying the windfall tax rate to the amount by which fair market value exceeds the regulated price.
and not a weakness of the position, as it only denies certain groups in society the luxury of directing government force against those unable to defend themselves in the political process.

C. **State Severance Taxes**

The third of the special taxes is the state severance tax of up to thirty percent "of the contract sales price" imposed by the state of Montana upon coal removed from the ground. The tax was sustained by the United States Supreme Court in *Commonwealth Edison Co. v. Montana*. The tax in question was levied upon all coal so removed, whether from federal or from state lands, and whether intended after sale for local use or for use in other states. The tax worked out to be about a seven-fold increase over the previous severance taxes—taxes based on tonnage and not on value—imposed by the state. The increased levels were explicitly justified by the Montana state legislature on the ground that the state held within its borders a portion of the low sulfur coal large enough so that demand for its coal would not dry up once the tax was imposed. In a manner reminiscent of the windfall profits tax, at least one-half of the monies collected were placed into a special trust fund, the principal of which could be spent only with the approval of three-fourths of the members of each house. The revenues generated by the tax were sufficient to permit Montana to reduce, as it in fact did, both its personal income and property taxes.

In the Supreme Court case, the challenge relevant here was that the tax offended the so-called negative implications of the commerce clause because it constituted a barrier to free trade between the states. In determining what these negative implications of the commerce clause are, the Court has made it very clear that the extreme position—no tax at all on goods in interstate commerce—cannot be sustained. Instead, operating under the credo that "[e]ven interstate business must pay its way," the Court fashioned rules which in some rough sense at least guarantee that goods in interstate commerce are not subject to any special burden from which local competitive goods are exempt. The economic rationale behind this general position is

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24 *Supra* note 22, § 15-35-101(e).
25 *Id.*, § 15-35-108(1).
26 *Id.*, § 17-6-203(5).
27 "The Congress shall have Power... To regulate Commerce... among the several States..." *U.S. Const.* art. I, s. 8, cl. 3.
28 The United States Supreme Court has been prepared to look at discriminatory regulations under the negative commerce clause. *Robbins v. Taxing District of Shelby County*, 120 U.S. 489, 30 L.Ed. 694, 7 S.Ct. 592 (1887).
clear enough, for the rule prevents the substitution from superior to inferior goods that would take place as a matter of course if taxes were imposed solely upon out-of-state goods. The general formulation of the rule was expounded in *Complete Auto Transit, Inc. v. Brady*,\(^{31}\) where it was held that a state tax does not offend the commerce clause if it “is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State.”\(^{32}\)

In this formulation, the first two elements are essentially irrelevant to our inquiry because they are always satisfied: everything turns on the last two. The fourth prong of the test restates in fairly clear form the general benefit test of taxation, which requires some commensurate benefit to the parties taxed. The third element, moreover, can be read in harmony with the fourth, if the element of “discrimination” in treatment is regarded as a rephrasing of the disproportionate impact test—our indirect measure of benefits provided for an admitted taking.

With this much said, the severance tax in question can be viewed from two vantage points. The first goes to federalism. It may be quite impermissible to have a court pass upon the tax under a negative commerce clause analysis. It is undisputed that Congress has full and plenary power to regulate the shipment of coal in interstate commerce, and, to achieve that end, to regulate the coal which remains in intrastate commerce as well. If there is some nation-wide outrage against the tax, the matter can be resolved in Congress, sparing the courts the heavy burden of intervention.\(^{33}\) The basic position can then be reinforced by a second observation that once a court gets into the business of striking down particular taxes it will never be able to extricate itself from the perils of standardless litigation.\(^{34}\) The reply to the first point is that the stakes are so high that coalitions amongst special interest groups will block sensible legislative action, so that judicial intervention to create the free trade zone is welcome as a matter of principle, here as in the many other cases where the negative powers have been invoked. The reply to the second is that underinclusive tests that permit the invalidation of some taxes should not be spurned if they admit of workable application solely because they cannot reach every abuse which state legislatures can contrive. A detailed analysis of the economic impacts of the taxes involved here is not necessary to condemn them on this ground. The obvious motive of the legislature in singling out a single commodity for differential taxation without so much as a colourable justification calls for at least some intervention.

This federalism question need not further detain us, as the tax may be

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\(^{32}\) Id. at 279 (U.S.), 1079 (S.Ct.).


\(^{34}\) For a forceful statement of this view, see Hellerstein, *Constitutional Limitations on State Tax Exportation*, [1982] A.B.F. Res. J. 1 at 55.
challenged from the second vantage point of individual rights: have any individuals, either the original owners of the coal or the purchasers thereof, been subjected to an uncompensated taking of their coal? On this matter, the general power of the Congress over commerce is of no importance. Instead, two questions of individual rights arise. The first asks whether individuals who are outside the taxing jurisdiction are required to pay special taxes for which they receive no comparable benefits. The second asks with equal force whether individuals within the taxing jurisdiction, who have some rights of participation in the local political process, are nonetheless victimized by its outcome.

As regards both producers and buyers, the ultimate issue of this eminent domain analysis is: was the tax fairly related to the services provided by the state? Looking at the matter in the abstract, it is clear that something must be amiss. If the original severance tax was proper, then it is doubtful that its replacement—seven times its size, and wholly different in its mode of collection—could well match the constant set of benefits provided by the state. It could of course be argued that the original tax furnished some sort of subsidy for the producers and consumers of coal in that the original rates were set too low. But as there is no indication of what services, apart from general police protection, were provided by the state, this possibility should be accepted only upon very strong evidence—evidence not to be found in the record of the case.

The Court in Commonwealth Edison did not, however, make the slightest pretence of identifying or valuing the services rendered by the state. Instead, the opinion at its critical point\textsuperscript{35} abandons the benefit test by quoting an extensive passage from Carmichael v. Southern Coal & Coke Co.,\textsuperscript{36} the gist of which is that “[t]he only benefit to which the taxpayer is constitutionally entitled is that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes.” But this simply will not do. By adopting some version of the benefit test, it must be understood that a given tax—or regulation—can in principle flunk the test so announced. Yet here there is no question but that every person will receive some scrap of benefit from every tax, however imposed, no matter how outlandish its rates, no matter how bizarre its purposes. Any inquiry into the operation and effect of a tax is barred in effect as long as society continues to function. The level of the benefit received for property taken should be treated as a question of fact, on which it is wholly improper to erect a conclusive presumption of adequacy. Yet after the value of benefits received is made relevant, then this tax must fail. Unless there is some special benefit of the severance tax to the owners or purchasers of the coal beyond the provision of the usual police protection and the like, already paid for by other taxes, then the tax must be struck down.

To satisfy the benefit test, it might be urged that the increase in the

\textsuperscript{35} Supra note 23 at 628 (U.S.), 2960 (S.Ct.).

\textsuperscript{36} 301 U.S. 495 at 522, 57 S.Ct. 868 at 878-79 (1937).
value of the mined coal increases the value of the state services rendered to the aggrieved parties. So much can be conceded, but it will not save this severance tax under the sensible tests announced for passing on its validity. If it turns out that coal properties are far more valuable because of the increased demands for energy than they were before, there are at least two ways that the state can capture its fair portion of that increase in value without resorting to the special severance tax. It can tax the increased amount of the gain on sale as part of the general income tax; as the gain increases so will the tax dollars collected. Or it can in more powerful fashion capture the gain as part of the general sales tax—roughly comparable for all commodities—or as part of a real estate tax based upon overall valuation, which is not, it must be added, restricted to those minerals which are severed from the ground, but which reaches all those which are in place. With these principled alternatives available, there is no reason to sanction the imposition of a tax, be it on producers or consumers, which is wholly abusive.

*Commonwealth Edison,* then, is an easy case given any rough estimate as to the match between the benefits and the burdens of the tax. Nor are matters better if disproportionate impact is the only ground upon which the tax could be struck down. Here again it is necessary to distinguish the position of the producers from that of the out-of-state consumers. With regard to the former, it seems clear that the portion of the tax which producers cannot pass forward is a disproportionate and therefore prohibited burden. In essence, the argument is that the national market in coal is highly competitive so that, where existing contracts themselves do not call for an automatic pass through of the tax increase, the producers will have to absorb most, if not all of the tax, in order not to lose sales to producers elsewhere.  

The argument for consumers is a bit more complex. Here on first appearance it might seem that there was no illicit discrimination because the tax was, as the Supreme Court noted, the same on local consumers as on out-of-state ones. But this wholly ignores two points. First, where the taxes are passed through under prior contracts, there is the strong likelihood of disproportionate burden unless it can be also shown that coal sold in domestic markets is subject to the same type of contractual provision. The second point applies to all these contractual arrangements. Of critical importance here is the parallel reductions in income and property taxes for local residents only. These reductions were made possible not by a reduction in internal state spending, but by the increase in the revenues derived from the severance tax upon coal. To be sure, the severance tax was imposed upon coal used for internal consumption as well. But the key point is that the two taxes were part of an integrated plan. So viewed it is clear that the decrease in the local income and property taxes functioned as a rough equivalent of a rebate to the severance tax. Here there will be no perfect correlation in the reduction of property and income taxes and the increase in severance taxes, but the match is close enough, especially since it is only local citizens who have a chance, not to say a near certainty, of participating in the windfall.

37 See Hellerstein, *supra* note 34 at 30; Williams, *supra* note 33 at 291.
If the tax reforms are taken as a package, as they were no doubt viewed in the legislature, the severance tax must be condemned not because it is discriminatory in itself, but because it was part of a comprehensive plan whose impact was disproportionate. On this view, therefore, the question of how much of the tax is passed forward and how much is not is quite immaterial. No matter which view of the transaction is taken, some group of individuals—it matters not whether they are local producers or out-of-state consumers—is subject to illicit burdens.

What then are the permissible powers of taxation? Here I do not suggest that some excise tax could not be imposed upon coal. As a first approximation, it is clear that the state is in fine shape if the tax it imposes is no greater than the sales tax which it imposes upon other commodities. As a further refinement, additional taxes could well be justified by showing that there are certain greater burdens imposed upon the state by the removal of coal from the ground—although none are even suggested in Commonwealth Edison. What is prevented is a justification for tax that quite simply asserts—as did Montana—that the state may tax its coal because it wants the revenue very much. To make that argument is to insist not upon sovereign control held over all property by the state but the private ownership of this coal by the state. It is therefore to confiscate by assertion alone. The moral for Canada should be obvious. The division of proceeds over the sale of Canadian oil should not be regarded solely as a political power struggle between the provincial and federal governments. Where the oil in question is in private hands (as is the case with roughly twenty percent of the Albertan oil) neither the provincial nor the federal government should be allowed to subject it to special discriminatory taxes. Where the ownership is vested in the province of Alberta, the federal government should not engage in partial acts of confiscation by subjecting that oil to special federal charges. Unless it can find some way to undermine the original distribution of rights, its claim to the oil rests upon greater might, not superior right.

D. Canada and the United States: Price Controls and Foreign Investment

The general principles used to distinguish the permissible from impermissible forms of taxation and regulation have thus far been illustrated exclusively with materials drawn from the American experience. The principles themselves, however, are subject to no particular territorial limitation. Even though the constitutional framework of Canada is quite different from that of the United States, the normative portions of the arguments survive even if the textual portions of the argument do not. Indeed, the normative element of the discussion is, if anything, somewhat more important in a system without entrenched individual rights: when everything is left within the political domain, legislative self-restraint has a greater importance than it does in a constitutional democracy.

With this said, it seems clear that in Canada, as in the United States,

38 Alberta has retained ownership and extraction rights in petroleum and natural gas in most public land devised to private owners. See the Public Lands Act, R.S.A. 1980, c. 297, s. 34.
the ideal of self-restraint has not been able to survive the massive shock to the political and economic systems resulting from the energy crisis. At one level, the arguments are on grounds of economic policy that are not tied to the system of individual rights referred to above. As a matter of policy, the best thing that any government can do in response to sudden and unanticipated shifts in the prices of vital goods brought on, say, by a cartel, is nothing—nothing at all. Inaction by the government will make it clear that private responses to the external changes are required, and these in turn can be made with greater accuracy in light of the reduced political uncertainty. On the demand side, major individual efforts can find substitute ways of doing business that blunt the effect of the price rise. On the supply side, alternative forms of energy, previously uneconomical, become viable financial propositions under the price umbrella created by the cartel. Some might think that this prescription is too dramatic, for an alternative, imposing tariffs on the importation of foreign oil, might capture domestically some of the cartel rents. But the tariff levels must be precisely set, and there is always the risk that domestic producers, with expenditures of real resources, will be able to keep them in place even after the cartel ceases to function. The temptation to fine tune the response to external shifts in market conditions should therefore be resisted; cartels should be left to fall of their own weight. Institutions like OPEC will become mired in frustration when they are unable to control markets as they had done in earlier years. This process of degeneration has taken place in the last year or two. It could have begun even sooner if the American government had just kept its hand out of the energy business.

The point of this essay is not to elaborate, however, what I think to be the appropriate choices that I as a policy analyst should choose to make. It is, instead, to identify the appropriate normative boundaries to the set of permissible choices. When, therefore, I criticize both American and Canadian forms of price control over crude oil, I do not do it solely on the ground that I think them inefficient. I do so also on the ground that the system of controls depends for its very survival on the government confiscating large sources of private wealth without compensation. The great battles over state, provincial or federal regulation—of which Commonwealth Edison is but one—are only debates over which level of government should be allowed to confiscate the most from private hands. If a government—Canadian, American, state, provincial, federal—wants to get into the business of regulating the price of oil and gas alone, it can do so by simply buying at market prices as much oil and gas as it chooses to, paying for supplies purchased out of the general revenue funds. If thereafter it chooses to sell the oil and gas at below-market prices on some type of rationed basis, it has not offended the normative principles against confiscation even if it has engaged in a policy which is for a variety of economic reasons wholly self-destructive. Placing this burden of purchase upon the government would make clear the real costs of its programmes at a very early stage, such that the likelihood that the policy would continue

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39 Since the Conference at which this article was presented, there have been major cuts in both prices and outputs in the spring of 1982, further confirming the general position taken here.
becomes remote in the extreme. Yet even this prediction should not be confused with the normative judgment. If it is thought that some symbolic, political or national concern justifies this general loss of both liberty and wealth, then the state can pursue this to the bitter end, so long as it does not resort to selective pressures against one group of individuals.

There is of course another alternative to price controls over crude oil. The government could simply confiscate outright some portion of the oil in place and then dispose of it as it sees fit. Here there is an issue of equity in theft, for the outright confiscation could be of the total ownership interests of some, or it could be spread pro rata over the ownership interests of all. The difference in incidence simply determines who is entitled to protest the takings involved, for even a widespread confiscation of oil, without reciprocal benefits to the owners, can in no way convert confiscation into a legitimate form of government action. Notwithstanding the strong moral case against this form of action, there is something to be said on its behalf, not in comparison to the proper system of purchase, but in comparison to the confiscation occurring under the applicable price regulations. Quite simply, straight confiscation interferes far less with the operation of markets than does the alternative system of price regulation. The government takes its oil interests and exploits them to maximize the wealth of the whole, confining its distribu- tional decisions to matters with little or no effect upon the productive side of the enterprise. The government simply becomes an owner or partner in certain oil interests. The only reason that this is not done is because the overt nature of the confiscation makes it impossible to conceal its illicit nature behind a fog of words. Governments always prefer the hidden taxes that should be condemned for sound institutional reasons. The indirect forms of confiscation are therefore preferred even though they are less efficient because they make plausible a government denial of the truth which has great symbolic value for most of us, who do not want to face the hard moral questions raised by its conduct. The system thus runs by an internal, if destructive, logic that no intellectual clarification can displace.

A parallel analysis is appropriate for another recent form of Canadian regulation, which unlike price controls over crude oil, is not found in the United States. I refer to the elaborate system of review which is established under the Foreign Investment Review Act (FIRA). In essence, the statutory plan is designed to tolerate further foreign investment into Canada in whatever form only if an administrative board determines that the proposed investment will provide, all things considered, some "significant benefit to Canada..." The tests which are used to determine this particular result cannot be purely economic. If they were, there would have to be a well-nigh conclusive presumption against a system which in turn will reduce the levels of employment and economic activity within the country. To be sure, a scheme with this far reaching impact must confer a net benefit upon a few individuals, but these will be quasi-monopolists who, protected from foreign

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40 S.C. 1973-74, c. 46 as am. by S.C. 1976-77, c. 52, s. 128.
41 Id., s. 2(1).
competition, will be able to market inferior goods and services at higher prices. No one can question the power of any nation to take strong steps whenever there is a substantial threat to its own national welfare and safety. But it is quite premature to assume that foreign investment in productive activities ever presents that sort of immediate threat. In almost every conceivable case, all important interests of national security can be effectively protected by a more tailored set of restrictions.

The question still remains, however, whether there can be any principled challenge to the FIRA on moral grounds. As regards future investment of foreign capital, these seem to be minor. The disadvantage wrought by the statute is advertised in advance, so that foreigners can steer clear of even approved investments if they think that the supplemental investments, necessary to the success of their overall plans, will be blocked by Canadian administrative actions. Canadians will share in whatever political or symbolic benefits are generated by the actions in more or less equal proportions. Without the direct measure of gains and losses, the non-discriminatory effects of the statute save it from a powerful moral attack.

There is, however, one class of claimants who have a more powerful case against application of the statute on normative grounds: the individual foreign firms which have already made investments prior to the passage of the statute. The issue was raised as a matter of statutory construction in Dow Jones & Co. v. Attorney-General of Canada,\(^42\) where the Court had to decide whether the statute applied to the transfer of a Canadian subsidiary from one non-Canadian company to another. Dow Jones, an American corporation, in a complicated set of transactions designed to obtain favourable tax treatment under American law, acquired Irwin U.S., an American corporation, and its wholly-owned Canadian subsidiary, Irwin Dorsey. It was agreed on all sides that the statute in question did not reach Dow Jones' acquisition of Irwin U.S. as such, but only the acquisition of its Canadian subsidiary, Irwin Dorsey. The Court held that the transaction was nonetheless caught by the notice and reporting provisions of the statute. The Court was obviously concerned about charges of retroactive application of the statute, which it thought unfounded:

> There can be no doubt that the Act is not retroactive in that it does not affect acquisitions of control of Canadian business enterprises which had been fully accomplished by non-eligible persons before the Act came into force unless and until that business is resold to another non-eligible person.\(^43\)

It then answered the possible charge of discrimination under the statute as follows:

> No distinction is made in the Act between an acquisition by such [non-eligible] persons of a Canadian-owned business and an acquisition from one who is a non-eligible person but who obtained such control before the Act was in force or from a non-eligible person who obtained the required consent after the Act came into force.\(^44\)


\(^{43}\) Id. at 400.

\(^{44}\) Id.
As a matter of principle, however, these observations, although true, do not meet the challenge. With respect to investments already made, the rules of the game have been changed in mid-play in ways that necessarily decrease the value of foreign holding of Canadian property. Whereas once there was a robust market for the shares of the foreign corporations, today that market is effectively limited to Canadian purchasers. It is true that Canadians are subject to the same restriction when they seek to sell to foreigners, but the Canadian companies, in addition to symbolic benefits, continue to enjoy two rights that the statute systematically denies to foreign corporations: a Canadian company can always make fresh infusions of capital, and it can acquire the Canadian subsidiary of a foreign corporation without approval. It therefore has both special rights and special duties; the foreign corporation only has special duties. The entire position can, moreover, become more distressing if there is any concerted pressure on the part of Canadian or provincial government officials to induce the foreign shareholders of the Canadian companies to sell their shares at distress prices, as by other forms of tax or regulation.

Looking therefore at the FIRA as a whole, its review procedures function as a powerful instrument to force the shift of existing investment from foreign to Canadian hands at below-market prices. While the general depressing effects of this legislation on the Canadian economy may be only cause for lamentation, its application to existing foreign investment is but another form of confiscation.

III. CONCLUSION

The purpose of this paper has been to draw attention to the question of which forms of government control should be regarded as within the domain of permissible policy choices, and which should be regarded as disguised confiscations. In dealing with this theme, it is quite clear that while all forms of regulation and taxation are subtle forms of the taking of private property, they are not necessarily confiscatory in and of themselves. Instead they are subject to two forms of justification: the police power and implicit in-kind compensation. There is within the American framework some faint recognition that the problem can be analyzed in this particular fashion, which is however followed by the implicit conclusion that with taxes and economic regulations the broad terrain of the prima facie case is fully occupied by its two principled exceptions. The point of this article is to show that in the context of recent retroactive and special legislation there are instances in which the prima facie case is not blunted by these two exceptions, even when broadly construed. The propositions in question are illustrated by consciously taking easy cases in which state conduct should in principle be attacked as illegitimate (in the Canadian context) or as illegitimate and unconstitutional (in the American context). As an historical matter, government legislation of this form has been with us for a long time. The greater stakes of modern regulation give the issue a new urgency, but do not require any change in either the analysis or outcome. Unchecked confiscation, total or partial, is always inconsistent with the ideal of limited government.