THE CONSTITUTION AND NATURAL RESOURCE REVENUES

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The last decade has witnessed dramatic political battles over the division of the vast revenues to be derived from Canada's rich natural resources. In this paper, John Whyte analyzes the central constitutional ambiguities which have underlain these struggles and which still remain unresolved. He examines the constitutional status of three key instruments by which

1 INTRODUCTION

Even the most casual observer of Canadian political life has been able to discern that over the last half decade political cleavages within Canada have not only been deep but until recently were effective in frustrating the development of needed national policies. Although it is not unique for a country to experience conflict over competing and irreconcilable views about its policies for the future, what made the heart beat faster, at least for constitutional lawyers, was that the Canadian conflict was rooted in different conceptions of the basic constitutional order.

On both major political fronts, constitutional reform and resource revenue sharing, truces or partial truces have been reached. The area of conflict with which this paper is concerned – the problem of dividing the revenues from non-renewable resources – is one in which none of the constitutional issues have been finally resolved. The Canada-Alberta Energy Agreement,[1] signed on September 1st, 1981, and the subsequent British Columbia and Saskatchewan agreements[2] will quiet some aspects of the debate for some years, but the basic question of the constitutional limits of provincial resource revenue taking remains.

There are three methods by which governments may obtain direct fiscal benefit from resource extraction. First, they may tax the benefits derived from mining the resources. Second, to the extent they own the resources, they may exact a rent from enterprises to which they give the right to extract the resource. Third, they may assume an entrepreneurial role and

There are, of course, other indirect benefits which governments may seek to gain from resource extraction within the boundaries of the province, state or country. Attempts to acquire these benefits (or reduce the economic and social costs which accompany this "blessing") are also subject to constitutional constraints. In fact, the single biggest blow to provincial constitutional economic regulatory powers in recent years came

2 TAXATION

of the other, but rather that excessive taxation is colourably regulatory.)

The general pattern of constitutional interpretation is further [illegible]

taxes are historical categories of direct tax, while import and export taxes, taxes on gross income or on production and commodity taxes are recognized categories of indirect tax. If a tax fits a recognized category, it is classified as direct or indirect accordingly. If it does not fit, the court will resort to the general test.

The other textual limitations of provincial taxation are that the taxation must be within the province and must be for "the raising of a revenue." Both these limitations have been hypothetically put forward to strike down resource taxes.[10] But in respect of both phrases, when the argument, which would be advanced by a taxpayer challenger, is considered it is seen to be less based on the words of section 92(2) and more on the claim that the tax entrenches on the federal power to regulate trade and commerce. The lesson to be learned, therefore, is that exercises of the provincial power to tax revenues from resources, unless constructed mindlessly, should not overrun the basic grant of provincial taxing power. On the other hand, the effect produced by such taxes can produce a different constitutional result: if taxes substantially interfere with

approximately the same level as the price per barrel received by producers prior to the oil embargo and price escalation. The tax scheme allowed some deductions, under approval of the Minister of Mineral Resources, for increases in production costs and extraordinary transportation costs. As a device to counter tax avoidance the Minister was given power to determine the well-head value of the oil when he was of the opinion that oil had

export price of oil. Two critical comments may be made. First, it is not

the producer is compelled to sell the oil which he produces. In an effort to obtain for the provincial treasury the increases

It is contended that the imposition of these taxes will not result in an increase in the price paid by oil purchasers, who would have been required to pay the same market price even if the taxes had not been imposed, and so there could be no passing on ... This, however, overlooks the all important fact that the scheme of the legislation under consideration involves the fixing of the maximum return of the Saskatchewan producers at the basic well-head price per barrel, while at the same time compelling him to sell at a higher price. There are two components in the sale price first the basic well head price

Saskatchewan, daunted but not resigned after this decision, enacted The Oil Well Income Tax Act[23] (commonly called Bill 47) with retroactive provisions which allowed the retention of the $500 million collected under

constitutional needs of provinces with significant energy resources, it did contain a provision for provincial [redacted]

another part of Canada and production not exported from the province.

In other clauses of the new section 92A provinces are granted exclusive legislative authority over development, conservation and management of natural resources.[26] These provisions may not be so much a novel grant of powers as an amplification of powers already enjoyed by provinces under existing provisions of the British North America Act.[27] In any event, this constitutional grant, or recognition, could conceivably have the effect of immunizing resource specific taxes from the attack based on the

Earlier I advanced the view that the [redacted]

General of Canada[34] that section 121's purpose is to create a general prohibition on restraints on the movement of products.[35] And elsewhere in the same opinion he implicitly identifies section 121 as being concerned with "interference with the free current of trade across provincial lines."[36] Under this view of the section there is a potential limitation on the provinces' contracting powers.

The power to make laws in relation to Crown minerals is conferred upon

that the Province may be in the same position as the original Province [redacted]

over resource revenues includes the ability to change the terms of the contract whenever the province chooses. Under Alberta law, all Crown leases are subject to two signficant features: the first is that the lessee agrees to deliver his oil to the Alberta Petroleum Marketing

4 STATE FIRMS

GENERAL

To the extent that a province wishes to become an entrepreneur in the oil and gas industry it is able to exert a considerable influence over the province's share of resource revenues. This is true whether the provincial enterprises derive revenue from Crown lands, freehold lands acquired since Confederation (or in the case of the Prairie provinces, since 1930) or from lands worked under mineral leases. There seems to be no constitutional limitation on a province's capacity to create Crown corporations through which provincial monies are dedicated to the acquisition or creation of commercial enterprises. It is true that the

provincial taxation power is limited to raising of revenue for

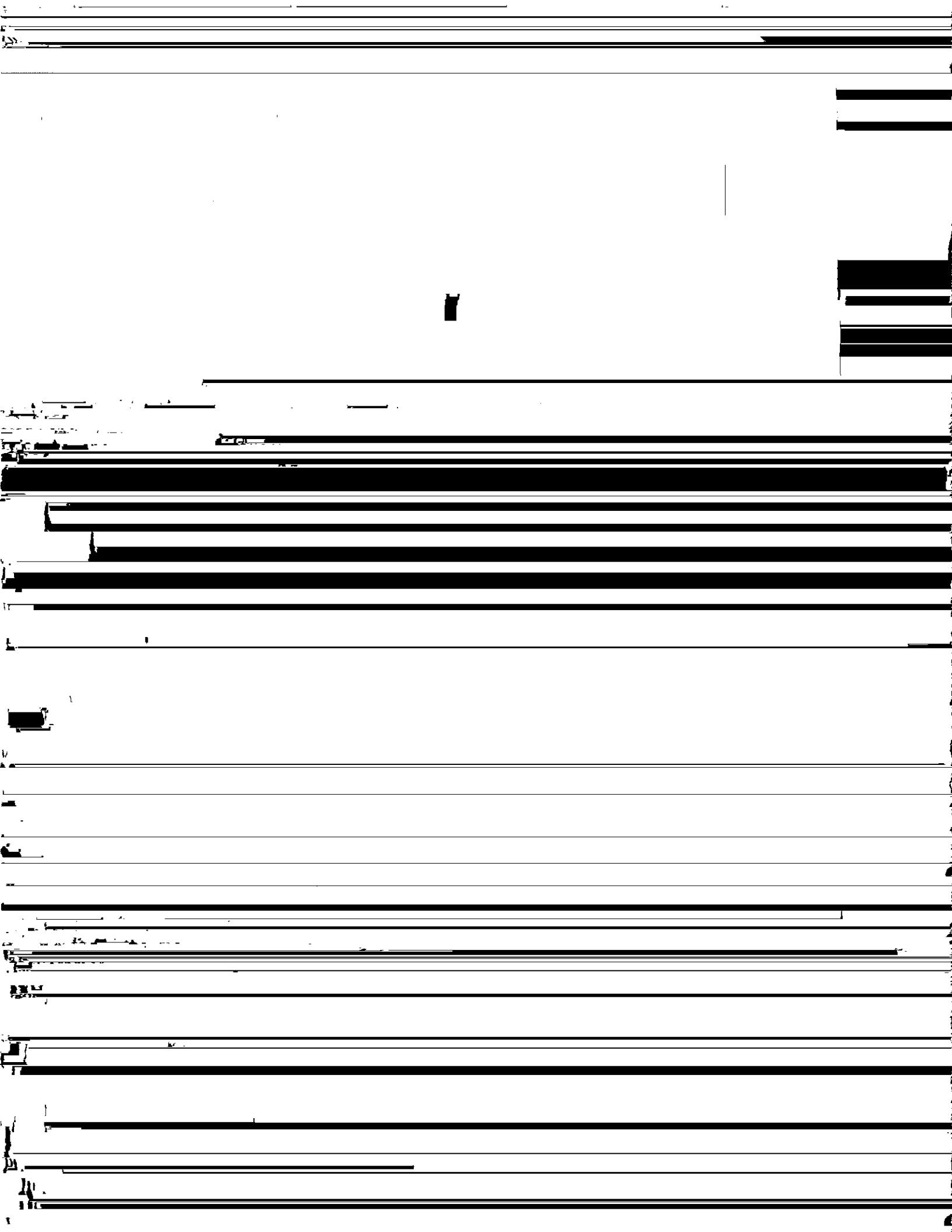
becoming involved in the industry. This is an issue of purely academic relevance at the present time since there seems to be an adequate capacity

for provinces to become engaged in the field through contractually based activity. In fact, the only circumstance under which expropriation would be a necessity is if a province were to set, as its policy, state ownership of the entire industry within the province. Twice in the last two decades British Columbia has passed legislation designed to "nationalize" an industry (that is, establish a state monopoly for either the whole province or a part of the province). The courts disallowed the first attempt, the B.C. Power Corporation case,[42] and permitted the second, the Insurance case.[43] The attempt which failed, however, failed because the expropriation was of a single company which was the sole asset of its federally incorporated parent. It was held that British Columbia's

permissible provincial policy notwithstanding the largely inter-provincial and international trading of the products of that sector.

THE SECTION 125 PROBLEM

The major constitutional issue bearing on the operation of state firms



as burdened with questions concerning the meaning and scope of the section 125 tax immunity as they might have been, the recent confrontation has underscored the growing importance of this issue. Federal ambitions to subject all non-renewable resource revenues to a uniform federal tax regime will not have evaporated with the signing of the energy pricing

or duty, was in fact an instrument of federal legislation allowable under a head of section 91 other than section 91(3) — the taxation power.

In Attorney General of British Columbia

protect government property only from 'taxation' and not from regulation

used in the Johnny Walker case, would not likely succeed. Although these

the government of a province. There seems to be little doubt about the

control actually exercised by the provincial government over the subsidiaries were as great as that exercised over the parent corporations the courts would likely fasten upon the separate legal existence of the subsidiaries as distinct corporations. Likewise, the statutory designation of these subsidiaries as agents of the Crown may not be effective in immunizing them from federal taxes. The subsidiaries would

Supreme Court of Canada), the producing provinces could turn major portions of their oil and gas industries into Crown

case since in that case the province's liquor retailing activity was motivated, at least in part, by a desire to capture the profits of that business. Furthermore, it cannot be argued that the distinction was not thought of in that case since Mr. Justice Idington, in the Supreme Court of Canada, in his decision, noted that the province's activity could not

"nationalization." Perhaps the answer might be found in the suggestion from the Mineral Water case that when the activities of the State are paralleled by "the like business of the citizen" (or in other words, when the Crown corporation acts in competition with the private sector in a particular market) intergovernmental tax immunization ought not to be

the purpose of the test or distinction (i.e., to prevent broad erosion of the federal tax base) would be defeated. In turn the result of this could well be that courts would begin to determine which provincial monopolies were "valid" and which were "invalid." Courts would undertake assessments

What is "Property" Within Section 125?

There are two aspects to this question. The first aspect is to discover the nature of the property which is mentioned in the section and the second is to determine whether some tax bases may be considered not to amount to a tax on property.

With respect to the first of the

since that section simply states that lands belonging to the pre-Confederation provinces shall belong to the post-Confederation provinces. In this way, the section identifies specific lands and constitutionalizes ownership of them. Its basic function is not to delineate the concept of ownership, but to confer a specific ownership. The result is that if the property referred to in section 125 is restricted to section 109 property, section 125's immunity relates only to those specific lands.

There is a further potential test for classifying property under section

decision of Snow v. The Queen,[69] it would seem that the possibility of providing a rational test whereby the tax could be seen as not burdening property but only burdening, say, a transaction, is not high. In the Alberta Reference,[70] the Alberta Court of Appeal rejected the attempt to classify taxes in this way:

> Section 125 refers only to lands or property. It does not expressly relate to taxes on persons or on transactions or on

5 CONCLUSION

It will be seen that in respect of interjurisdictional tax immunity the

addressed by the courts. Governmental activity and economic conditions which have permitted these issues to go unresolved for so long are quickly changing; section 125 jurisprudence can be expected to be an important factor in the sharing of resource revenues by governments.

governments, such as Canada has had, normally proceed through equal part of self-confidence and ambition. The question that remains open is whether the considerable provincial resource powers will serve to keep the tension alive, to hold up the present balance between the centre and the regions. If so, resources may be serving a double duty in Canadian development: enhancing its economic growth and, through federal-provincial conflict over resources, producing long term political stability.

NOTES

1 Memorandum of Agreement between the Government of Canada and the Government of Alberta relating to Energy Pricing and Taxation, September 1, 1981. Paragraph 14 of the Agreement states:

(b) development, conservation and management of non-renewable natural resources and forestry resources in the province, including laws in relation to the rate of primary production therefrom; and
(c) development, conservation and management of sites and facilities in the province for the generation and production of electrical energy.

This new section may not significantly improve the constitutional position of provinces since provincial laws respecting "development, conservation and management" may so markedly affect international trade that courts will ascribe a federal character to them rather than a s. 92A character.

Federal-Provincial Dimensions of the 1973-74 Energy Crisis in Canada" in W. Oates, The Political Economy of Fiscal Federalism (Lexington: Lexington Books, 1977) 105-113; Moull, supra note 10, at 11-12;

laws in relation to matters coming with the classes of subjects next hereinafter enumerated; that is to say ...

34 [1958] S.C.R. 626.

35. Id. at 637-643. [redacted]

acting for or on behalf of Her Majesty in right of Canada or a province.

have been obtained under the NGGLT and COSC in respect of the Crown in right of Saskatchewan, its agents, and every person acting for or on behalf of the Crown in right of Saskatchewan. The grants shall include a payment forthwith to the Government of Canada of a grant in lieu equivalent to all amounts (including interest thereon as calculated by Revenue Canada) that would have been payable to date from November 1, 1980 under the provisions of the NGGLT and COSC by the Crown in right of Saskatchewan, its agents, and every person acting for or on behalf of the Crown in right of Saskatchewan.

The Government of Saskatchewan agrees to provide to the Government of Canada all the information and other material that would have been required under the provisions of the NGGLT and COSC.

8. **Payment of the Petroleum and Gas Revenue Tax (PGRT) and the Incremental Oil Revenue Tax (IORT)**

The Government of Saskatchewan takes the position that the Crown in right of Saskatchewan, its agents, and

in lieu of the PGRT and IORT in the amounts and at the times that are equivalent to those that would have been obtained under

frank concession by British Columbia to pay federal taxes will weaken any argument based on s. 125 which it may wish to make at the expiration of the agreement or in respect of some other sectors of provincial governmental activity.

63 Report of the Parliamentary Task Force on Federal-Provincial Fiscal Arrangements, **Fiscal Federalism in Canada**, (Ottawa: Department of Supply and Services, 1981) 191.

64 W. McConnell, **Commentary on the British North America Act** (Toronto: MacMillan of Canada, 1977) 369.

65 **Supra**, note 54, at 380. Brodeur, J. in the same case, however, did refer to Idington, J.'s distinction between governmental and commercial functions. He did not reject the distinction but said that the direct sale of liquor was the final step in the evolution of a public policy relating to liquor consumption (at 391).

66 199 U.S. 261 (1905).

67 326 U.S. 572 (1946).

68 Id., at 588-589.

69 (1979), 102 D.L.R. (3d) 191 (Federal Court of Appeal), affirming (1979), 92 D.L.R. (3d) 71 (Federal Court Trial Division).

70 **Supra**, note 46, at 16.

71 See J. Corry, **My Life and Work: A Happy Partnership** (Kingston: Queen's University, 1981) 226-236 for an exposition on the [illegible]

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