1890

Legislative Tax-Exemption Contracts

Ernest W. Huffcut

Indiana University School of Law

Follow this and additional works at: http://www.repository.law.indiana.edu/facpub

Part of the Jurisdiction Commons, Legislation Commons, and the Tax Law Commons

Recommended Citation


http://www.repository.law.indiana.edu/facpub/1990

This Article is brought to you for free and open access by the Faculty Scholarship at Digital Repository @ Maurer Law. It has been accepted for inclusion in Articles by Maurer Faculty by an authorized administrator of Digital Repository @ Maurer Law. For more information, please contact wattn@indiana.edu.
LEGISLATIVE TAX-EXEMPTION CONTRACTS.

I. The Question Stated.
II. Legislative Contracts in General.
III. Irrevocable Tax-Exemption Contracts.
IV. Opposition to the Doctrine.
V. Limitations and Applications of the Doctrine.
  1. Exemption will not be Presumed.
  3. Exemption a Personal Privilege and not Transferable.
  4. Exemption of One of Two Consolidated Companies does not Exempt Both.
VI. The Tendency of the Court.

I. THE QUESTION STATED.

The sovereignty of the state is essentially indivisible and inalienable. In the last analysis it reposes in the people themselves. It may be granted to a single individual. It may be delegated to public representatives. It may be lodged in co-ordinate branches of government. Two or more states may even by mutual consent yield the exercise of specified powers to a joint government, and thereby limit the extent, though not the content, of their individual sovereignty. But in all these cases the incidents of sovereignty are given into the hands of public officers, and the same power that granted may revoke. Once lodged, the sovereignty remains until recalled. In no case is it conceivable that these temporary trustees can transmit to others the trust that they have received, or give, grant or barter away any of its essential powers.

In our modern representative governments this principle is practically conceded. Whatever is non-essential or incidental may be the subject of legislative gift or contract, but whatever is essential and of the essence of sovereignty is lodged permanently in the people and can be disturbed only with their consent. If one legislature, by gift or contract, attempt to dispose of any of these essentials, no right vests in the beneficiary other than the right of present enjoyment subject to the pleasure of...
the same or a subsequent legislature. Blackstone has stated the rule broadly that "acts of Parliament derogatory from the power of subsequent parliaments bind not," putting the rule upon the ground that "the legislature, being in truth the sovereign power, is always of equal, always of absolute authority." 1 And the rule is equally sound under our republican form of government, subject only to the limitation that the legislature is not, like the British Parliament, an omnipotent body, but is amenable always to the constitution, and must act within the well defined limits of that instrument. But nowhere in any American constitution is there to be found any authority under which a legislature can barter away the essentials of sovereignty. The founders of the republic would have stood amazed at any proposition looking to that end. While individual States were asked to yield up certain of the incidents of sovereignty to be exercised in their behalf by a superior government of which they were a part, they retained in undiminished vigor all rights and power not expressly granted. These they exercise within their respective jurisdictions with the same absolute freedom and under the same political sanction as if wholly independent states. And these, or such of these as are essential to their separate political existence, they cannot dispose of or in any way abridge, and still remain sovereign states.

While the rule is thus broad and inclusive there has been in one particular a wide and dangerous departure from it in the course of American jurisprudence. The Supreme Court of the United States has established and thus far maintained the doctrine that a State can by contract yield for a term of years or forever its right of taxation. It is conceded that it cannot thus bind itself to an irrevocable contract for the non-exercise of the right of police 2 or of eminent domain, 3 powers certainly not

1 1 Black. Com. 90. See also Williams v. Pritchard, K. B., 4 T. R. 2, a tax case in which it is said: "It cannot be contended that a subsequent act of parliament will not control the provision of a prior statute, if it were intended to have that operation;" also Perchard v. Heyward, K. B., 8 T. R. 468.


3 Cooley, Const. Lim., pp. 281, et seq., 525; West River Bridge v. Dix, 6 How. 507.
more important or of higher rank in the scale of sovereign attributes than the right of taxation. It may, therefore, well be asked on what theory and by what process of reasoning the courts have come to establish this one notable exception to so sweeping a rule. To point out the origin of the doctrine of irrevocable tax-exemption contracts, the reasoning upon which it rests, the opposition with which it has been received, and the limitations with which it has been hedged about, will be the object of this paper.

II. LEGISLATIVE CONTRACTS IN GENERAL.

In the absence of constitutional restrictions a State legislature would wield such absolute sway as to be able to make and break contracts at will. This follows naturally from the character of the legislative power. It was, indeed, questioned by the eminent jurist, Chief Justice Marshall, "whether the nature of society and of government does not prescribe some limit to the legislative power," but he concedes in the same breath that the problem is practically insoluble. In Dartmouth College v. Woodward, he says: "According to the theory of the British constitution, their Parliament is omnipotent;" and in Owings v. Speed, he refused to protect the beneficiary of a legislative grant from the operation of a subsequent act divesting such beneficiary of his title under the grant, and placed the decision on the ground that previous to the adoption of the Federal constitution there was no check on the supreme power of a State legislature except such as might exist in the constitution of the State itself. Other decisions in the Federal courts have re-affirmed the same doctrine.

It may be broadly asserted that a legislature, untrammeled by constitutional checks, is practically omnipotent.

It next becomes important to inquire what checks, if any, have been placed upon the power of a legislature to make, enforce, or revoke contracts. It is not our purpose to deal with such restraints as have been imposed in State constitutions, but only

1 Fletcher v. Peck, 6 Cranch, 87, 135.
2 4 Wheat. 518, 643.
3 5 Wheat. 420.
4 League v. De Young, 11 How. 185.
with the clause of the Federal constitution under which acts of State legislatures relating to contracts have been repeatedly annulled. The first clause of the tenth section of article I of the constitution of the United States provides that "no State shall * * * pass any bill of attainder, ex post facto law, or law impairing the obligation of contracts." Under this clause there has grown up a series of judicial decisions remarkable not only for their great learning but also for the incalculable effect that they have had upon important public and private interests. It is to these that we must look for the law in restraint of legislative action concerning contracts.

The phrase, "impairing the obligation of contracts," is attributed, upon just what authority is uncertain, to Judge Wilson, a Scottish lawyer profoundly learned in the civil law and one of the ablest members of the Constitutional Convention. It was first proposed in the convention to adopt a somewhat similar clause from the Ordinances for the Government of the North-West Territory, which provided that "in the just preservation of rights and property, it is understood and declared, that no law ought ever to be made, or have force in said territory, that shall, in any manner whatever, interfere with or affect private contracts or engagements, bona fide and without fraud, previously formed." This proposition did not meet with favor, and the clause as it now stands was finally adopted.

Just what the convention meant to guard against in making this phrase a part of the fundamental law, has been the subject of much learned discussion. The subject was scarcely mentioned during the heated controversy that followed the completion of the work of the convention. It is referred to but twice in the Federalist, once by Hamilton in No. VII. of that famous collection, and once by Madison in No. XLIV. When it first came up for interpretation by the Supreme Court the journal of the convention and the Madison papers yet lay in manuscript and were inaccessible; Judge Wilson, its probable author, was dead; and the court, to quote Chief Justice Marshall, decided the question from "the meaning of words in common use." Probably the court employed the best resources at its command, but the student of our judicial history will, in the light of subsequent
events, read with some surprise the able Chief Justice's assertion that "it would seem difficult to substitute words which are more intelligible or less liable to misconstruction," and that "the words of the constitution are express, and incapable of being misunderstood." 1 From all the evidence thus far adduced, it seems altogether probable that the framers of the constitution meant simply to place a prohibition upon State legislation impairing the obligation of private contracts, and to set up in civil cases the same safeguard as is provided in criminal cases by the clause forbidding the passage of ex post facto laws. 2 But whatever the intention of the authors of the clause, the courts gave to it so elastic an interpretation as to bring within its scope all contracts, executed and executory, private and legislative.

The question of legislative contracts first came up with reference to a grant of land made by the State of Georgia to private individuals and afterwards revoked on the ground that the grant had been obtained by fraud. Chief Justice Marshall delivered the opinion of the court and settled once for all these propositions: (1) a grant by a State is a contract; (2) a contract with a State is within the prohibition of the clause of the constitution forbidding a State to pass any law impairing the obligation of contracts. 3 This doctrine of irrevocable legislative grants was soon after re-affirmed. 4

From the doctrine of irrevocable grants of corporeal property, the court passed to that of the irrevocable grant of franchises. Charters of incorporation were held to be contracts within the intent of the constitution and to be beyond the future control of the law-making power. This doctrine was first enunciated in the now famous case of Trustees of Dartmouth College v. Woodward, 5 and has been repeatedly re-affirmed. 6

Thus, under this clause of the constitution, intended doubtless for the protection of private contracts from legislative interfer-

1 Sturges v. Crowninshield, 4 Wheat. 122, 197, 198.
2 See Shirley's The Dartmouth College Causes, pp. 213-228.
3 Fletcher v. Peck, 6 Cranch, 87.
4 Terrett v. Taylor, 9 Cranch, 43; Town of Pawlet v. Clark, 9 Cranch, 292, 335.
5 4 Wheat. 518.
ence, there grew up the doctrine that a legislature can make a contract so binding as completely to tie the hands of all subsequent legislatures, so immovable that it can never be disturbed, amended, or repealed. The result has been far from favorable to public interests. Established without warrant of precedent or tradition, the doctrine has become so settled and stringent in its application, so comprehensive and far-reaching in its scope, that under its protection, to quote the words of one of the ablest of modern commentators, "the most enormous and threatening powers in our country have been created; some of the great and wealthy corporations actually having greater influence in the country at large than the States to which they owe their corporate existence. Every privilege granted or conferred—no matter by what means or on what pretense—being made inviolable by the constitution, the government is frequently stripped of its authority in very important particulars, by unwise, careless, or corrupt legislation; and a clause of the Federal constitution, whose purpose was to preclude the repudiation of debts and just contracts, protects and perpetuates the evil." 1

As we shall see presently, in no respect is this unwise legislation more frequent or pernicious than in the granting of tax-exemption contracts, and one of the justices of the Supreme Court has borne witness that it is this class of contract cases that "most frequently calls for the exercise of our [their] supervisory power." 2

III. IRREVOCABLE TAX-EXEMPTION CONTRACTS.

The case of the State of New Jersey v. Wilson, 3 decided in 1812, is the first of a long line of cases dealing with legislative contracts as to taxation. The circumstances of the case were briefly as follows: The Delaware Indians had, in 1758, yielded their claim to certain portions of New Jersey under an agreement by which they were to be forever secured in the possession of a tract of land of about three thousand acres to be purchased for

1 Cooley's Constitutional Limitations, p. 279, note.
2 Murray v. Charleston, 96 U. S. 432.
3 7 Cranch, 164.
their use and to be exempted from taxation. They resided on this tract until 1801, when the remnant of the tribe secured the passage of an act whereby they were empowered to sell the land and migrate to an Indian settlement in New York. This enabling act contained no provision whatever on the subject of taxation. The lands were sold in compliance with the act, and passed into the possession of private individuals. Soon afterward the legislature repealed the provision of the act of 1758 relating to taxation, and efforts were made to levy and collect the prescribed taxes. The owners of the land brought suit to test the validity of the repealing act, and, after the courts of New Jersey had decided adversely to them, carried the case to the Supreme Court of the United States where it was submitted without argument. Chief Justice Marshall read the opinion of the court re-affirming the doctrine of Fletcher v. Peck, that the constitutional prohibition extends to contracts to which a State is a party as well as to contracts between individuals; holding that the act of 1758 constituted a contract, and that the privilege of exemption from taxation was annexed to the lands and not to the persons of the proprietors; and deciding that as the State of New Jersey did not insist on the surrender of this privilege in the enabling act of 1801, the purchasers under that act acquired all the privileges and immunities enjoyed by the Delawares. The subsequent act intended to annul this exemption was therefore adjudged unconstitutional on the ground that it impaired the obligation of the original contract.

Whatever may be thought of the other cases held to fall within the prohibitory clause concerning contracts, there can be no question but that this involved consequences of the gravest character, and gave form to a series of judicial decisions that have met with strong and well grounded opposition. It was probably the first time in the history of jurisprudence that the sovereign power of taxation had been adjudged the proper subject-matter of contract. So imperative a necessity exists for the exercise of this power, that it is of the very essence of political autonomy. To hold that one legislature can forever bind the State to the non-exercise of this prerogative, is to hold that the legislature can destroy the State by taking from it the means of existence.
It will be shown later how the Supreme Court shrank from the logical consequences of its own decision, and how sundry of the judges refused further assent to so dangerous and irrational a doctrine.

Fortunately we are not left in doubt as to the attitude of the present court toward this leading case on tax-exemption contracts. In 1885 exactly the same state of facts came before the court. It appears that for a long period of years after the decision in New Jersey v. Wilson, the owners of the exempt tract contented themselves with the right to an extraordinary privilege and failed to insist upon its exercise. But after the lapse of sixty years some owner of a portion of the exempt land again asserted his right to immunity from taxation, and refused to pay his assessments. This led to the important determination to be found in Given v. Wright. Mr. Justice Bradley, speaking for the court in that case, says:

"We do not feel disposed to question the decision in New Jersey v. Wilson. It has been referred to and relied on in so many cases from the day of its rendition down to the present time, that it would cause a shock to our constitutional jurisprudence to disturb it now. If the question were a new one we might regard the reasoning of the New Jersey judges as entitled to a great deal of weight, especially since the emphatic declarations made by this court in Providence Bank v. Billings and other cases, as to the necessity of having the clearest legislative expression in order to impair the taxing power of the State."

"The question then, will be whether the long acquiescence of the land-owners under the imposition of taxes, raises a presumption that the exemption, which once existed, has been surrendered."

And on this last ground, thus painfully sought out that the leading case might stand undisturbed, the court decides that, as the original exemption was a franchise and as taxes have been assessed and paid for sixty years, the non-user of the franchise for that period amounts to "presumptive proof of its abandonment or surrender."

While the decision in New Jersey v. Wilson was thus open to criticism, its full significance was not seen until another, and more famous case, had been adjudicated in the highest court of the republic.

The decision in the Dartmouth College Case gave to the tax-exemption contract doctrine an instant and tremendous importance. That decision, as everybody knows, declared that the charter of a private corporation is a contract and within the protection of the constitution of the United States. The inevitable conclusion followed that an exemption from taxation contained in a charter creating a corporation, is a part of such charter and partakes of its inviolability. It was speedily seen by those interested that a rule of law which was adopted to protect a deserving charity could be as easily invoked to protect a moneyed corporation or a greedy monopoly. Corporations have been swift to avail themselves of the knowledge. Under the aegis of the Dartmouth College Case the most oppressive monopolies have sheltered themselves from the legislative action of the very power to whose indulgence they owe their existence. Attempts of legislatures to cut off or of courts to curb the dangerous exercise of corporate franchises have invariably been met by an appeal to this decision; and it is not too much to say that corporations may justly claim the famous document as their historic Magna Charta. The words of Chief Justice Richardson in reading the opinion of the New Hampshire court have, after the lapse of seventy years, almost the ring of prophecy:

"If the charter of a public institution, like that of Dartmouth College, is to be construed as a contract within the intent of the constitution of the United States, it will, in our opinion, be difficult to say what powers, in relation to their public institutions, if any, are left to the State. It is a construction, in our view, repugnant to the very principles of all government, because it places all public institutions of all the States beyond legislative control." 1

In the face of all these considerations the Supreme Court held

---

1 Farrar's Report of the Case of Dartmouth College, etc., p. 230; also, 1 N. H. Rep. 111.
the charter of a corporation a more sacred thing than the sovereignty of a people. All English law and precedents were thrust aside. In England the right of Parliament to dissolve a corporation or to amend its charter had never been successfully questioned.¹ The creature of law, owing its life to the breath of legislative or royal favor, it was amenable throughout its existence to its creator. The most powerful corporations,—like that known as the East India Company,—yielded their charter rights and even their corporate life at the will of Parliament. But in the United States another doctrine was solemnly promulgated. Existing corporations, the term of whose life was not fixed by their charters, might truly claim the attribute of immortality. States were warned that if they wished to maintain any control over future corporations, they must do so by reserving that right in all charters thereafter granted.² In a word, the attempt of the framers of the constitution to protect the sanctity of contracts had been broadened into a foundation for the most obnoxious monopolies.

The case of the Piqua Branch of the State Bank of Ohio v. Knoop³ is of great importance as containing the first thorough discussion of all questions involved in legislative tax-exemption contracts. The State of Ohio had in 1845 passed a general banking act, one provision of which was that each banking company organized under the act should semi-annually set off six per cent. on its net profits in lieu of all taxes to which the company or the stockholders therein would otherwise be subject. The Piqua Branch was organized under this act in 1847. In 1851 the legislature passed an act “to tax banks, and bank and other stocks, the same as property is now taxable by the laws of the State.” A tax was levied upon the Piqua Branch Bank under this act and upon the bank’s refusing payment, suit was brought by the State for its enforcement. The bank set up as a defense that the tax imposed was in violation of its charter. The Supreme Court of Ohio sustained the validity of the tax, and the case was appealed to the Supreme Court of the United

LEGISLATIVE TAX-EXEMPTION CONTRACTS.

States. Here a decision was given in favor of the bank, the opinion being read by Mr. Justice M'Lean, the sole survivor, as he pathetically remarks in the course of his opinion, of the famous bench of judges of which Marshall and Story were leading lights. The opinion is learned and exhaustive, conceived in the spirit of Marshall's earlier decisions, and buttressed with much of that great master's invincible logic. It had previously been decided in Gordon v. Appeal Tax Court that an annual bonus in lieu of taxation, fixed by the charter of a banking corporation and accompanied by a pledge not to tax such corporation beyond the extent of the bonus, was a contract binding on the State and operating in favor of the stockholders personally as well as of the corporate capital. In the case now under consideration there was no pledge that such annual per cent. of profits should be forever accepted in lieu of other tax, nor did the question of individual taxation of stockholders come before the court. The majority of the court, concurring with Mr. Justice M'Lean, held that the law of 1845 created a contract binding on the banks established under it and on the State; and that the act of 1851 impaired the obligation of that contract and was therefore unconstitutional and void.

The feature of the opinion which must make it of lasting interest to all students of this subject, is the argument that a State, in granting an irrevocable exemption from taxation does not relinquish a part of its sovereign power. The learned justice says:

"The assumption that a State, in exempting certain property from taxation, relinquishes a certain part of its sovereign power is unfounded. The taxing power may select its objects of taxation; and this is generally regulated by the amount necessary to answer the purposes of the State. Now the exemption of property from taxation is a question of policy and not of power." 2

And again:

"A State in granting privileges to a bank, with a view of affording a sound currency or of advancing any policy connected with the public interest, exercises its sovereignty, and for a pub-

---

1 3 How. 133. 2 16 How. 384.
lic purpose, of which it is the exclusive judge. This act so far from parting with any portion of its sovereignty, is an exercise of it. Can any one deny this power to the legislature? Has it not a right to select the objects of taxation and to determine the amount? To deny either of these, is to take away State sovereignty." 1

This argument is specious but, it seems to us, fatally weak. It is true that the exemption of property from taxation is a question of policy. It is equally true that the legislature may and should exempt property from taxation whenever there is a sound reason for so doing. The encouragement of religion and morals, the advancement of education, even, as the learned justice suggests, the providing for a sound currency,—all these objects and many more may justify a legislature in granting exemptions from taxation. And it is true, likewise, that a legislature in so doing does not part with any portion of its sovereignty. Anglo-Saxon legislatures in all ages have done these very things. But always, and everywhere, save under the judicial interpretations of our own court, such grants have been made with the understanding that they could be re-called as the needs or policy of the State might dictate. A legislature in exempting church property from taxation parts with no portion of the State sovereignty; but a legislature that attempts to exempt the same property forever from taxation does attempt to part with a portion of the State sovereignty. The sovereign power of taxation is the absolute power to tax every kind and all of every kind of property within the jurisdiction of the taxing power. Anything less than this is something less than sovereignty. Therefore the legislature of Ohio did not part with any portion of the sovereignty of that State in accepting a per cent. on profits in lieu of taxation, but it did part with a portion of the sovereignty in binding all subsequent legislatures to accept the same arrangement.

It is easy to see that such a doctrine might be carried to the verge of State suicide. Suppose, for instance, in the case of New Jersey v. Wilson, cited above, that a great city with a mill-

1 16 How. 389.
ion inhabitants had grown up within the limits of the exempt land. These citizens, together with millions of property, would have been forever free from taxation for State purposes in virtue of an arrangement with the Delaware Indians made over a hundred years ago. If banks may be exempted from taxation, so may railroads, and manufactories, and farms, and property of every description; and it needs only a corrupt and worthless legislature in order to tie forever the taxing power of the State in regard to the most extensive private interests. The exigencies of a State can never be foreseen. As well might a legislature say that a certain piece of property shall forever be exempt from the possibility of lawful seizure under the right of eminent domain, as to say that it shall forever be exempt from taxation. A contract could be made, and a consideration paid, in one case as well as in another. But such a law would be no more a contract than would a law forever yielding the right of the State to exercise the police power over the same property. A legislature may always select the objects of taxation and determine the amount; it may, from considerations of public policy, exempt certain kinds of property from all taxation whatever; it may consent to receive a fixed amount in lieu of regular taxation; but it cannot, without yielding up sovereign attributes, make a binding contract, for a term of years or forever, the subject-matter of which is the power to tax.

As will be pointed out more in detail later, a strong minority of the court took this view of the case and dissented strongly from the doctrine of the prevailing opinion.

The case just under consideration was decided in 1853. From that time down to the present moment the question has returned again and again to trouble the court, and will continue so to return until an indispensable prerogative of sovereignty is vindicated against the strength of blind precedent. It is needless to traverse the ground covered by the later decisions further than to point out the extent to which the doctrine has been carried.

Two important cases, — The Home of the Friendless v. Rouse and The Washington University v. Rouse, may be considered.
together, as both arose out of the same state of facts. Both were cases where charitable institutions had been chartered with a provision exempting them from taxation and had afterward been subjected to taxation by a subsequent legislature. Mr. Justice Davis, speaking for the court, says:—

"The validity of this contract is questioned at bar on the ground that the legislature had no authority to grant away the power of taxation. The answer to this position is, that the question is no longer open for argument here, for it is settled by repeated adjudications of this court, that a State may by contract based on a consideration, exempt the property of an individual or corporation from taxation, either for a specified period or permanently. And it is equally well settled that the exemption is presumed to be on sufficient consideration, and binds the State if the charter containing it is accepted."

It would be difficult to find a plainer statement of the law established by the Supreme Court of the United States on this important question, or one more welcome to corporate interests.

To this decision there were also dissenting voices, as we shall see when we come to a fuller consideration of the opposition with which the doctrine of irrevocable tax-exemption contracts has been met.

In all subsequent cases the question has been treated as res adjudicata, although the court has from time to time expressed doubts as to the wisdom of the established doctrine. In the case of Wilmington Railroad v. Reid 1 and Raleigh and Gaston Railroad Company v. Reid, 2 the question was so treated and no dissenting voices seem to have been heard. In the course of his opinion in the former case, however, Mr. Justice Davis, speaking for the court, says:—

"It may be conceded that it were better for the interest of the State, that the taxing power, which is one of the highest and most important attributes of sovereignty, should on no occasion be surrendered. In the nature of things the necessities of government cannot always be foreseen, and in the changes of time, the ability to raise revenue from every species of property may be

1 13 Wall. 264.  2 13 Wall. 269.
of vital importance to the State, but the courts of the country are not the proper tribunals to apply the corrective to improvident legislation of this character. If there be no constitutional restraint on the action of the legislature on this subject, there is no remedy, except through the influence of a wise public sentiment, reaching and controlling the conduct of the law-making power."

Other cases of like character have been frequently before the court during the last score of years, but the decisions have been uniformly consistent with the leading cases.¹

IV. OPPOSITION TO THE DOCTRINE.

The doctrine laid down in the leading cases on the right of one legislature to grant exemption from taxation which shall bind all subsequent legislatures, has not been established without strong and persistent opposition. A slight survey of the circumstances attending the decision of a few of these cases will amply sustain this proposition.

The first case, that of New Jersey v. Wilson,² was submitted without argument and, as is intimated in Given v. Wright,³ might have been very differently determined upon a fuller consideration of all the facts. The questionable nature of the subject-matter of the supposed contract in that case, namely, the sovereign prerogative of taxation, does not seem to have occurred to Chief Justice Marshall; at any rate, it receives no attention in his opinion. But the subject of taxation was brought forcibly to his attention in the famous case of M'Culloch v. Maryland,⁴ decided a few years afterward, and again in the case of Osborn v. United States Bank.⁵ In these cases, while deciding in favor of the supremacy of the laws of Congress and against the rights

---

² 7 Cranch, 164.
³ 117 U. S. 648, 655.
⁴ 4 Wheat. 316.
⁵ 9 Wheat. 738.
of the States to tax "its instruments employed in the execution of its powers," he enforces the truths that, "the power of taxation is one of vital importance;" that "the power of taxing the people and their property, is essential to the very existence of government, and may be legitimately exercised on the objects to which it is applicable, to the utmost extent to which the government may choose to carry it;" that "the people of a State give to their government a right of taxing themselves and their property, and as the exigencies of government cannot be limited, they prescribe no limits to the exercise of this right, resting confidently on the interest of the legislator, and on the influence of the constituents over their representative, to guard them against its abuse." 1 Here was a statement of principles which might have carried the learned Chief Justice to a different decision in New Jersey v. Wilson, had they been clearly before him in the consideration of that case. They were before him, as we shall presently see, in the consideration of Providence Bank v. Billings,2 decided in 1830,3 and doubtless did much to induce the rule of construction in that case which has ever since controlled the Supreme Court in its adjudication of tax-exemption causes. These two cases, New Jersey v. Wilson and Providence Bank v. Billings, comprised the law as it was established by Chief Justice Marshall and his associates, and as it has continued, practically unimpaired since their day. But the opposition, as already stated, has been strong and persistent.

In the case of the State Bank of Ohio v. Knoop 4 three justices, Catron, Daniel and Campbell, dissented, and Chief Justice Taney refused his assent to the doctrine of the controlling opinion, although he concurred in its conclusions. Two of the justices, Catron and Campbell, wrote dissenting opinions. The dissent of Mr. Justice Catron rests mainly upon the proposition, boldly asserted and strenuously maintained, "that, according to the constitution of all the States of the Union, and even of the British Parliament, the sovereign political power is not the sub-

---

1 4 Wheat. 428. 1819; and Osborn v. U. S. Bank in 1824.
2 4 Pet. 514.
3 New Jersey v. Wilson was decided in 1812; McCulloch v. Maryland in 1819; and Osborn v. U. S. Bank in 1824.
4 16 How. 369.
ject of contract so as to be vested in an irrepealable charter of incorporation, and taken away from, and placed beyond the reach of, future legislatures; that the taxing power is a political power of the highest class, and each successive legislature having vested in it, unimpaired, all the political powers previous legislatures had, is authorized to impose taxes on all property in the State that its constitution does not exempt." ¹

The dissenting opinion of Mr. Justice Campbell goes to the same point, but with such firmness of logic and with such force of statement, as to make it the "leading opinion" among a large and increasing number of dissenting voices on this important question of constitutional law. A few extracts will show the nature and scope of his argument.

"The powers of that assembly in general, and that of taxation especially, are trust powers, held by them as magistrates, in deposit, to be returned after a short period, to their constituents, without abuse or diminution.

"The nature of the legislative authority is inconsistent with an inflexible stationary system of administration. Its office is one of vigilance over the varying wants and changing elements of the association, to the end of ameliorating its condition.

"The subject-matter of this section [of the law of 1845 previously referred to] is the contributive share of an important element of the productive capital of the State to the support of its government. The duty of all to make such a contribution in the form of an equal and apportioned taxation, is a consequence of the social organization. The right to enforce it is a sovereign right, stronger than any proprietary claim to property. The amount to be taken, the mode of collection, and the duration of any particular assessment or form of collection, are questions of administration submitted to the discretion of the legislative authority; and variations must frequently occur, according to the mutable conditions, circumstances, or policy of the State." ²

We shall see later that these sound principles of government have since received the sanction of another strong and determined minority of the Supreme Court. It is safe to say that a

¹ 16 How. 404.
² 16 How. 407.
large majority of the profession would give their assent to the proposition laid down in these opinions of the minority of the court.

In an opinion given in another case at the same term, Chief Justice Taney says that while he concurs in the judgment of the majority of the court in State Bank of Ohio v. Knoop, he dissents from the reasoning on which the decision rests. His own views are explained in the following extract:

"Powers of sovereignty confided to the legislative body of a State are undoubtedly a trust committed to them, to be executed to the best of their judgment for the public good; and no one legislature can, by its own act disarm their successors of any of the powers or rights of sovereignty confided by the people to the legislative body, unless they are authorized to do so by the constitution under which they are elected. They cannot, therefore, by contract, deprive a future legislature of the power of imposing any tax it may deem necessary for the public service— or of exercising any other act of sovereignty confided to the legislative body, unless the power to make such a contract is conferred upon them by the constitution of the State."

In the case of The Home of the Friendless v. Rouse and Washington University v. Rouse three of the eight judges sitting strongly dissented from the prevailing opinion. The three were, Chief Justice Chase and Justices Field and Miller, the last of whom wrote the dissenting opinion and entered a solemn protest against the dangerous doctrine that was to receive a new sanction in the case at bar. "To hold," he says, "that any one of the annual legislatures can, by contract, deprive the State forever of the power of taxation, is to hold that they can destroy the government which they are appointed to serve, and that their action in that regard is strictly lawful." In Pacific Railroad Co. v. McGuire, Justices Clifford and Miller disented and Chief Justice Waite put his assent upon other grounds than that the tax-exemption was a contract which a subsequent legislature could not impair. In Farrington v. Tennessee three judges, Strong,

1 The Ohio Life Ins. & Trust Co. v. Debolt, 16 How. 416, 431.
2 8 Wall. 430.
3 8 Wall. 439.
4 20 Wall. 36.
5 95 U. S. 679.
Clifford and Field, dissented from the prevailing opinion. Thus it will be seen that the doctrine that one legislature can forever tie up the hands of its successors in a matter of sovereign importance, was first enunciated in a case submitted without argument and decided without investigation, was afterwards rigidly limited by the same great jurist who promulgated it, and has since been repeatedly disaffirmed and rejected by a strong minority of the court who are firm in the belief that the doctrine must finally be abandoned.

V. LIMITATIONS AND APPLICATIONS OF THE DOCTRINE.

1. EXEMPTION WILL NOT BE PRESUMED. — Reference has already been made to the limitation of the doctrine of New Jersey v. Wilson in the subsequent case of Providence Bank v. Billings. It is now necessary to point out more specifically the nature of this limitation.

The Providence Bank was created under a charter which contained no provision whatever on the subject of taxation, but authorized the bank "to employ its capital in banking transactions for the benefit of the stockholders, and bound the State to permit these transactions and restrained it from passing any act that would destroy the profits of the bank. A few years later the legislature of Rhode Island passed an act taxing the bank and this was resisted by the bank on the ground that it impaired the obligation of the contract embodied in the charter. In the course of his opinion Chief Justice Marshall says:

"That the taxing power is of vital importance, that it is essential to the existence of government, are truths which it cannot be necessary to re-affirm. They are acknowledged and asserted by all. It would seem that the relinquishment of such a power is never to be presumed. We will not say that a State may not relinquish it; that a consideration sufficiently valuable to induce a partial release of it may not exist; but, as the whole community is interested in retaining it undiminished, that community has a right to insist that its abandonment ought not to be presumed in
a case in which the deliberate purpose of the State to abandon it does not appear." 1

The principle enunciated in this case received re-affirmation and sanction in the leading case of Charles River Bridge v. Warren Bridge. 2 The question there at issue was not one of exemption from taxation, but of exemption from competition, or in other words a question of monopoly. The charter of the Charles River Bridge Company contained no provision as to exclusive privileges; afterward the legislature granted to the Warren Bridge Company a franchise for erecting a bridge which would, at the expiration of a few years, become a free bridge, and thus destroy utterly the value of the Charles River Bridge Company's property. The latter company contended that its charter contained an implied contract on the part of the State not to grant to any other person any privileges which would destroy the value of its franchise. On this point Chief Justice Taney says:—

"The object and end of all government is to promote the happiness and prosperity of the community by which it is established; and it can never be assumed that the government intended to diminish its power of accomplishing the end for which it was created. * * * The continued existence of a government would be of no great value, if, by implications and presumptions, it was disarmed of the powers necessary to accomplish the ends of its creation, and the functions it was designed to perform, transferred to the hands of privileged corporations. * * * While the rights of private property are sacredly guarded, we must not forget that the community also have rights, and that the happiness and well being of every citizen depend on their faithful preservation." 3

The principle adopted in these two leading cases has continued to govern the court in its subsequent consideration of legislative grants. As we are particularly concerned only with grants of tax-exemptions, it will be unnecessary to do more than cite a few of the cases of that character in which the principle has been applied. Mention should be made of Mr. Justice Miller's com-

plaint that the court has "been, at times, quick to discover a contract that it might be protected, and slow to perceive that what are claimed to be contracts were not so by reason of the want of authority in those who profess to bind others." 1 While this charge is abundantly sustained by facts, it is, on the other hand, equally true that the court has been slow to discover legislative contracts where they rest in any degree upon implication. And indeed the court has carried this doctrine of strict construction of legislative grants to such a length, that Mr. Justice Miller finds himself constrained in a recent case to dissent together with Chief Justice Waite, and Justices Field and Bradley, from the prevailing decision of the court. The case is a peculiar one and worthy of careful study.

In 1853 the legislature of Louisiana granted a charter to the Vicksburg, Shreveport and Texas Railroad Company, the second section of which reads as follows: "The capital stock of said company shall be exempt from taxation, and its road, fixtures, workshops, warehouses, vehicles of transportation, and other appurtenances, shall be exempt from taxation for ten years after the completion of said road within the limits of the State." Owing to the fact that the completion of the road was delayed by the outbreak of the civil war, the State undertook to tax the property in use upon the completed portion, and the courts were called upon for a construction of the exemption clause. After reiterating the doctrine of Providence Bank v. Billings and other cases to the same effect, the court, speaking through Mr. Justice Gray, says: —

"In their natural and legal meaning, the words 'for ten years after the completion of said road,' as distinctly exclude the time preceding the completion of the road, as the time succeeding the ten years after its completion. To hold that the words of exemption used by the legislature include the time before the completion of the road would be to insert by construction what is not to be found in the language of the contract; to presume an intention, which the legislature has not manifested in clear and unmistakable terms, to surrender the taxing power; and to

1 Washington University v. Rouse, 8 Wall. 439, 442.
go against the uniform current of the decisions of this court upon
the subject."

From this construction of the exemption clause the four
judges already mentioned dissented, and concurred in the opin-
ion that "this exemption was designed to aid the road, and was,
therefore, much more needed during its construction than when
completed. It seems like a perversion of the purpose of the
statute to hold that it intended to impede by its burden the prog-
ress of the desired work, and relieve it of the burden only
when finished." It is significant that Justices Miller and Field
were the only judges taking part in the decision of the Home of
the Friendless v. Rouse and Washington University v. Rouse,
who were still on the bench when Vicksburg, etc., R. R. Co. v.
Dennis was decided. From the doctrine of irrevocable legisla-
tive tax-contracts established by the former case they strongly
dissented. From the severe application in the latter case of the
doctrine of strict construction in determining the meaning of
such contracts they dissented with equal earnestness. Radically
opposed to the doctrine in 1869, they find themselves the con-
servative members of the court in 1886. It is interesting, in
view of these facts, to speculate as to what would have been the
attitude of the court in 1886 toward the whole subject of tax-
exemption contracts had it come up as a new question and not
as a res adjudicata.

The court has, however, been thoroughly consistent in its
avowed purpose to construe all legislative grants strictly against
the grantee and to uphold no claims that rest on implication.
Thus, where one company was invested with the powers and
privileges and subjected to the obligations contained in certain
enumerated sections of the charter of another, and one of the

1 Vicksburg, etc., R. R. Co. v. Den-
nis, 116 U. S. 665. The principle is
fully affirmed in the case of Yazoo
The Massachusetts court has adopted
a far more liberal construction as may
be seen in Trinity Church v. Boston,
118 Mass. 164, where it was held,
under a statute exempting "houses
of religious worship," from taxation
that a lot purchased by a religious
corporation and upon which they had
driven piles for the foundation of a
building was so exempt. See also
New England Hospital v. Boston, 118
Mass. 518. This is, perhaps, as far as
any court has ever gone, even in con-
struing gratuitous exemptions.
Legislative Tax-Exemption Contracts.

Enumerated sections exempted that other company from taxation, it was held that the exemption did not pass to the new company.\(^1\) So, where by legislative enactment a railroad was to pay an annual bonus of \$10,000 and its stock was to be assessed to the amount of the costs of construction, it was held that subsequent legislation levying a general tax upon the gross receipts of all transportation companies applied to this railroad, and that the original plan of taxation was not a surrender of the right of the State to tax in any other way it might see fit.\(^2\) And other cases go to sustain the fixed doctrine that "the power to tax rests upon necessity, and is inherent in every sovereignty, and there can be no presumption in favor of its relinquishment."\(^3\)

2. Exemption without a Consideration is not a Contract. — A second and very important limitation of the doctrine of irrevocable tax-exemption contracts is to be found in the repeated decisions of the Federal Supreme Court that an exemption which is a mere gratuity, with no consideration passing from the beneficiary to the State, is not a contract and is repealable at the pleasure of the grantor. This was so decided in the leading case of Christ Church v. Philadelphia.\(^4\) In 1833 the legislature of Pennsylvania enacted that "the real property, including ground rents now belonging and payable to Christ Church Hospital, in the city of Philadelphia, so long as the same shall continue to belong to the said hospital, shall be and remain free from taxes." In 1851 an act was passed under which this property became subject to taxation. It was held that—

"The concession of the legislature was spontaneous, and no service or duty, or other remunerative condition, was imposed on the corporation. It belongs to the class of laws denominated privilegia favorabilia. It attached only to such real property as belonged to the corporation, and while it remained as its prop-

---

\(^1\) Railroad Company v. Commissioners, 103 U. S. 1.

\(^2\) Erie Railway Company v. Pennsylvania, 21 Wall. 492.


\(^4\) 24 How. 300.
erty; but it is not a necessary implication from these facts that the concession is perpetual, or was designed to continue during the corporate existence. Such an interpretation is not to be favored, as the power of taxation is necessary to the existence of the State, and must be exerted according to the varying condition of the commonwealth. The act of 1833 belongs to a class of statutes in which the narrowest meaning is to be taken which will fairly carry out the intent of the legislature."

The general statement is that such a stipulation between individuals "would belong to the category of nude pacts. It has no higher character because one of the parties was a State, the other a corporation, and it was put in the form of a statute." 1 Such acts amount frequently to mere bounty laws dictated by public policy, and determinable at the will of the legislature. Such was held to be the case where a State offered to exempt from taxation all real and personal property used in the manufacture of salt, and afterward limited the exemption to five years. But the court in that case stated that had the same provision been contained in a special charter, which the corporation had accepted and acted upon, it would have constituted a contract. 2 In other words, what would be an irrevocable contract under a special charter is a mere gratuity under a general law. 3

It was this same distinction between a contract and a gratuity that led to the majority decision in Home of the Friendless v. Rouse, 4 a decision that Mr. Burroughs in his valuable work on taxation 5 finds great difficulty in reconciling with the principle laid down in Christ Church v. Philadelphia. In the former case the exemption was granted by special charter "for the purpose of encouraging" the establishment of a charitable institution; in the latter case it was granted because it had been "represented that in consequence of the decay of the buildings of the hospital, and the increasing burdens of taxation, its means are curtailed and its usefulness limited." In the former case the corporation was induced to act on the promise of exemption; in the latter,

1 Tucker v. Ferguson, 22 Wall. 527, 574.
2 Salt Company v. East Saginaw, 13 Wall. 373.
3 Welch v. Cook, 97 U. S. 541.
4 8 Wall. 430.
5 pp. 115-117.
the corporation was simply relieved of burdens which it was lawfully required to bear.

While this distinction may serve to clear away the difficulties raised by Mr. Burroughs's objections, the exception taken by him to Mr. Justice Davis's *dictum* in the Home of the Friendless *v.* Rouse, that "it is equally well settled that the exemption is presumed to be on sufficient consideration," is certainly well grounded. It is now an elementary principle in all these cases that "the contract must be shown to exist," that "there is no presumption in its favor," and that "every reasonable doubt should be resolved against it." And every such exemption must be upon a consideration in order to constitute an irrevocable contract.  

3. **Exemption is a Personal Privilege and not Transferable.** — The general doctrine of irrevocable tax-exemption contract has received a further important limitation in the decision of the Supreme Court that such exemption is a personal privilege, does not attach *in rem*, and does not pass with the sale of the franchises and property of the original beneficiary. This important question was first squarely decided in the case of Morgan *v.* Louisiana, which has ever since been regarded as a leading authority. The legislature of Louisiana had in 1853 incorporated the New Orleans, Opelousas and Great Western Railroad Company with a clause exempting the capital stock from taxation forever, and the works, fixtures, rolling-stock and appurtenances, for the space of ten years after the completion of the road. The road was sold in 1869 on execution and passed into the possession of Morgan. The State afterwards sued Morgan for taxes upon the road and he set up as a defense the exemption clause of 1853. The question thus presented was whether, under the designation of franchises, the immunity from taxation upon property of the road passed to the purchaser. The Supreme Court decided that it did not, but that the exemption "was a mere personal privilege of the company, and, therefore, not transferable to others."

---

1 Tucker *v.* Ferguson, 22 Wall. 575.  
2 Cases cited *supra*; West Wisconsin Co. *v.* Supervisors, 93 U. S. 595;  
3 Home Insurance Company *v.* City Council, 93 U. S. 116.
The court in the same decision defined and fixed the meaning of the term "franchise," so far as such definition was necessary in the discussion of tax-exemption privileges. It said: —

"The term must always be considered in connection with the corporation or property to which it is alleged to appertain. The franchises of a railroad corporation are rights or privileges which are essential to the operations of the corporation, and without which its road and works would be of little value; such as the right to run cars, to take tolls, to appropriate earth and gravel for the bed of its road, or water for its engines, and the like. They are positive rights or privileges, without the possession of which the road of the company could not be successfully worked. Immunity from taxation is not one of them. The former may be conveyed to the purchaser of the road as part of the property of a company; the latter is personal, and incapable of transfer without express statutory direction."

The general principle enunciated in Morgan v. Louisiana has governed the court in all subsequent adjudications of the questions there involved, and has done much to limit the sweeping force of the leading cases. Yet this decision was not reached without a serious divergence from a former decision, and a divergence which has widened with the lapse of time. The former decision referred to is that in the case of Humphrey v. Pegues,¹ where the court held that a charter conferring on one company "all the powers, rights and privileges granted by the charter" of another company, carried with it the exemption from taxation enjoyed by the original company. To reconcile this decision with those of subsequent cases of a like character, has proved a troublesome matter. In Morgan v. Louisiana the distinction was placed on the ground that while immunity from taxation might pass under the term "privilege," it could not pass under the sale of "franchises." In Railroad Companies v. Gaines² the distinction was placed on the ground that while immunity from taxation might pass under a general grant of "all the powers, rights, and privileges," it would not pass under a similar grant limited by the words "for the purpose of making and using said

¹ 16 Wall. 244.
² 97 U. S. 607.
road." In Picard v. Tennessee, etc., Railroad Company, the court speaks of "the later" and "better opinion" "that unless other provisions remove all doubt of the intention of the legislature to include the immunity in the term 'privileges,' it will not be so construed." In short the strictest possible rule of construction has been followed in all cases subsequent to Morgan v. Louisiana, and the court has uniformly refused to uphold an alleged immunity from taxation where the franchises to which the immunity was originally attached had been transferred.

It may be stated as a general rule, supported by numerous cases, that immunity from taxation is a personal privilege, and does not attach to or run with the property or franchise, and is not transferable unless by a new and expressed authorization by the legislature.

4. Exemption of One of Two Consolidated Companies Does Not Exempt Both. — A new phase of the question is presented in those cases where two companies are consolidated, one of which is by law exempt from taxation and the other not. Of course here, as elsewhere, the plainly expressed intent of the legislature to exempt the new company formed by the consolidation, will be entirely conclusive. But in the absence of any statutory provisions, the rules of construction laid down by the courts will govern.

It may be stated broadly that where two companies are consolidated, each of which was exempt from taxation under its original charter, the new company will also be exempt unless the act authorizing the consolidation provides otherwise. In such a case the presumption is that the new company takes all the powers and privileges which were possessed by the two original corporations at the time of their union, and this presumption can be rebutted only by proving a contrary intention on the part of the legislature.

3 Tennessee v. Whitworth, 117 U. S. 244; Memphis R. R. Co. v. Commissioners, 112 U. S. 600; St.
In case one of the consolidated companies was exempt and the other not, and the act authorizing the consolidation provides that the consolidated companies shall possess all the rights and privileges which each of the companies enjoyed under its charter, the exemption from taxation extends only to that portion of the aggregated property which was, at the time of the union, exempt under the charter of the favored company. But even in such a case, the rule must be taken with the qualification that the new company possesses such transferred powers, privileges and immunities, only so far as they can be exercised and enjoyed by it, with its different officers and distinct constitution. Whenever the new corporation is not so constituted as to comply with this condition precedent to exemption or commutation of taxation, it can lay no claim to such privilege.

VI. The Tendency of the Court.

From this brief survey of the law of legislative tax-exemption contracts, it must be evident that there has been a marked change in popular, and even judicial, opinion since the cases of New Jersey v. Wilson and Dartmouth College v. Woodward were given to the world. At that time corporations were few in number and of inconsiderable importance. Since then there has been a remarkable increase in the number of corporations and a constant growth of corporate power. The exercise of such power in the corrupting of legislators and the procuring of legislation favorable to corporations and dangerous to public interests, and the alarming combinations and "trusts" which have been formed within the past few years, have justly excited public discussion as to the control of these bodies. It is altogether probable that this discussion will increase rather than diminish during the next score of years, and that the principles stated in the preceding


LEGISLATIVE TAX-EXEMPTION CONTRACTS.

pages will be again and again argued in the courts and before the people.

That the Supreme Court is alive to the necessity of a more stringent control of corporations may be clearly gathered from a study of the decisions in the "Warehouse Cases," the "Granger Cases," the "Railroad Commission Cases," and Spring Valley Water Works v. Schottler. So far has the court gone in these cases in order to leave the legislature free to control corporations, that a strong minority of the court and the great body of the profession have been unable to reconcile the cases with the principles laid down in Dartmouth College v. Woodward.

It is safe to say that this tendency will continue. It may even happen, as a not very remote contingency, that the court will depart utterly from the doctrine of the leading case. There are not wanting those who think that it has already gone far in that direction. But whatever may be the outcome as to general questions involved in charter rights, it has been predicted by a very eminent authority—Mr. Justice Miller—that the court will finally abandon altogether the doctrine that the taxing power can be restricted or destroyed by exemptions contained in corporate charters or other legislative contracts. While such a reversal of the leading cases would undoubtedly give an unpleasant shock to our judicial system, it may well be a matter of serious reflection whether, after all, it would not be in the interests of good government and an enlightened public policy.

MINNEAPOLIS, MINN.

ERNEST W. HUFFCUT.

1 94 U. S. 113.
2 94 U. S. 155, 164, 179, 180, 181;
108 U. S. 526.
3 116 U. S. 807.
4 110 U. S. 347.
5 8 Wall. 444.