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UNIVERSITY OF OTTAWA

# PROVINCIAL TAXATION POWERS IN CANADIAN CONSTITUTIONAL LAW

Thesis presented to the School of Graduate Studies of the University of Ottawa in partial fulfillment of the requirements for the degree of Master of Laws.

by

Joseph Magnet

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# PROVINCIAL TAXATION POWERS IN CANADIAN CONSTITUTIONAL LAW

Joseph Eliot Magnet

# P R E C I S

In Canada, the constitutional distribution of taxation powers was addressed to political problems which have long since become obsolete. The original distribution reflected the then accepted view that the Parliament of Canada was the pre-eminent legislative power. The grant of taxation powers to the provinces was thought to be insignificant. It was meant to severely limit provincial expenditure on the laissez fairetheory that the areas of social regulation committed to the provinces were insubstantial. This state of affairs has totally passed away in fact and in theory. The rearrangement of taxation powers which has resulted from judicial activity is largely a history of the inflation in provincial responsibilities.

The growth in provincial taxation power largely orbits around judicial interpretation of Sec. 92:2 of the B.N.A. Act. The courts early took as the central focus for interpretation of this clause an arcane phrase from John Stewart Mill's Principles of Political Economy. Of central significance has been the fact that the court held that the test by which direct and indirect taxation could be separated was a legal, and not an economic test. Since the test was put on this footing, the courts could be very tolerant of taxation which, historically understood, would have been considered indirect.

In fact, this is precisely what the courts have done. They have allowed provincial legislatures to levy to some extent hybrid taxes - taxes having effects both direct and indirect -

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and taxes which, while in the main are direct, produce collateral indirect effects. The chief way in which this has been done is by disregarding the economic effect of the taxation as it works its way through the economy. The courts search for the general tendency of the tax as commonly understood by plain men. In truth, this legal fiction has been used to enlarge provincial taxing competence. That this is so, has been expressly noted in recent judicial decisions.

A central argument submitted in the present work is that it is time to rethink the legal fictions upon which provincial powers of taxation have been built. It is suggested that the true restriction which the courts have developed in respect of provincial taxation is that the taxation not traverse the provincial border. In other words, direct taxation has ceased to be a term of utility, insofar as that term denotes the historical distinction to which Mill adverted. In practice, direct taxation has become a mere matter of form; the courts are very tolerant of the levying by provincial legislatures of indirect taxation so long as the legislatures restrict themselves to taxing within their own borders. The way in which this has been done is to allow provincial collateral powers of indirect taxation, and to uphold hybrid taxes.

The provinces have a second source of indirect taxing competence in the provincial licensing power. This is largely undeveloped for the reason that it has been difficult to discern how far the provincial licensing power comes as a direct exception to the prohibition that the legislatures refrain from

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indirect taxation. The commentators have largely discounted the licensing power; it has been maintained that the power has no independent force.

It is suggested in the present study that the provincial licensing power constitutes a discrete source of provincial collateral indirect taxation competence when used ancillary to a valid provincial regulatory scheme. The substantive restriction is that the scheme not be in relation to the raising of moneys by indirect taxation, but that the scheme be truly in relation to a valid source of provincial regulatory power. If levies are truly ancillary to a valid provincial regulatory scheme, the provincial licensing power is capable of supporting such levies even though, ex hypothesi, the direct taxation power is unavailable. Reinterpretation of old cases, as well as analysis of relatively recent law, support this view.

The distribution of taxation powers in Canada is incomplete. Certain interstices remain were neither legislature is competent. Sec. 121 is by far the most important constitutional plank in this scheme. The section is clearly in a state of flux although certain trends are emerging. It is suggested that the most appropriate framework for conceiving of the clause is to consider it in tandem with the federal commerce power, the powers thus combined providing a mechanism for holding safe from interference interprovincial streams of commerce. One difficulty in this analysis is the uncertainty as to the extent of such streams. It is suggested that Sec. 121 disables either level

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of government from inhibiting interprovincial streams of commerce which serve to reinforce purely provincial objectives. However, regulatory measures which seek to achieve the efficient allocation of resources are not within the reach of Sec. 121.

Two last vacuums in the taxing powers are examined. Sec. 125 holds safe from taxation lands or property belonging to Canada or a province. Judicial consideration of this clause has revealed that proper drafting is capable of diluting its effectiveness considerably. Finally, examination is made of case law which casts an absolute prohibition on taxes collected pursuant to ultra vires or inoperative statutes.

## I. INTRODUCTION

### 1. Historical

Immediately prior to confederation, British North America, though politically structured, was an economically decentralized cluster of small and scattered settlements.(1) Twenty percent only of its 3.5 million people lived in cities. Transportation difficulties were formidable and proved to be the main obstacle to development. This was intensified by a severe winter which annually closed all water routes for five months.

By 1866 the then Province of Canada and the municipalities had extended loans totalling $40 million to railway companies. The investments soured. There was a substantial public debt and poor public credit. The railway network was conceived on a continental scale; it was ill suited to the economic needs of the primarily agricultural Province of Canada.

After the Act of Union in 1841, Canada became responsible for her own defence. British troops were withdrawn. American pressure on the western territories became severe. The Northern Pacific Railway, chartered by Americans in 1864, had the

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1. See generally: Report of the Royal Commission on Dominion-Provincial Relations (Ottawa, 1940), I, 19-46; Moore, Perry & Beach, The Financing of Canadian Federation: The First Hundred Years (Toronto: Canada Tax Foundation, 1966), pp. 1-16; Lynn, Federal Provincial Fiscal Relations, Studies of the Royal Commission on Taxation number 23, (Ottawa: Queen's Printer, 1967), pp. 43-50; Safarian, Canadian Federalism and Economic Integration (Ottawa: Information Canada, 1973), pp. 15-18.

2. See Report of the Royal Commission on Dominion-Provincial Relations, op. cit. f.n. 1, p. 20.

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object of providing transcontinental service. American settlement was pushing ever northward. Without the protection of British troops, American expansionist claims to the west seemed impossible to resist.

The scheme of Confederation was principally designed to overcome these problems. It was thought that a larger, strongly centralized political unit would be capable of (1) re-establishing the public credit, (2) undertaking the considerable public expenditure on transport which was condition precedent to development, and (3) offering a sufficient defence posture to resist American pressure.

2. Constitutional Distribution of Taxation Powers

Cultural and sectional rivalries proved insuperable obstables to the legislative union forseen by MacDonald. A federal state, characterized by strong cultural and regional guarantees, was the compromise. But there was to be no question of economic decentralization.[3] By the B.N.A. Act, 1867[4] the Dominion government was granted legislative power over:

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3. "On peut maintenant tenter de definir ce que fut la fédération canadienne à ses debuts. Elle fut avant tout un compromis entre le groupe qui désirait une forte centralisation et même une union législative pour des raisons économiques et le groupe qui insistait sur la décentralisation pour préserver la diversité des cultures et des conceptions sociales. En général, on peut dire que les deux groupes ont gagné leur point et que, en tenant compte de la signification limitéede ces termes à l'époque, la politique sociale, y compris l'administration de le justice, décentralisée...[Les provinces] pedaient les principales fonctions économiques de l'Etat à cette epoque au profit de gouvernement fédéral..." Lamontagne, Le Fédéralisme canadien (1954), p. 12.

4. 30 and 31 Vict., c. 3.

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"91(3) The Raising of Money by any Mode or System of Taxation."

By S. 122 of the Act customs and excise, which accounted for the vast bulk of public revenue immediately prior to confederation, were brought within the central government's exclusive competence. Sec. 118 of the Act, since repealed, (5) made provision for payment of subsidies by the central government to the provinces, stated to be "in full settlement of all future demands on Canada". In the early years of Confederation such subsidies accounted for some fifty per cent of all provincial revenues.

These provisions left no doubt in the minds of the founders that the Dominion would have the pre-eminent power of taxation. Both the Quebec and London Resolutions declared that the payment of subsidies to the provinces was "in consideration of the transfer to the General Parliament of the powers of taxation." (6)

The B.N.A. Act granted powers of taxation to the provincial legislatures too. These were not considered significant. It was thought that provincial activities would be circumscribed and revenue needs slight; the legislatures, accordingly, would have no need to resort to most tax pools. (7) Therefore, by Section 92 of

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5. Statute Law Revision Act, 1950, 14 Geo. VI, c. 6 (U.K.).

6. Quebec Resolutions no. 64, London Resolutions no. 62.

7. Canadian Industrial Gas and Oil Ltd. v. Govt. of Sask. (1978), 80 D.L.R. (3d) 449 (S.C.C.)

the B.N.A. Act, the legislatures were restricted to:

> "2. Direct Taxation within the Province in order to the raising of a Revenue for Provincial Purposes.
>
> ....
>
> 9. Shop, Saloon, Tavern, Auctioneer, and other Licenses in order to the raising of a Revenue for Provincial, Local or Municipal Purposes."

One of the overriding ideas of the Confederation scheme was the creation of a large free trade area in which strong industry could develop and prosper. This fundamental principle was constitutionally expressed by S. 121 of the B.N.A. Act, which reads:

> "121. All Articles of Growth, Produce or Manufacture of any one of the Provinces shall from and after the Union, be admitted free into each of the other Provinces."

The last constitutional provision of current significance is Section 125. This contemplates restrictions of substance which grow out of the realization, noted by Chief Justice Marshall, that "the power to tax involves the power to destroy".(8) The restrictions ensure that taxing powers will not be used to upset the framework of Confederation. Section 125 provides:

> "125. No Lands or Property belonging to Canada or any Province shall be liable to Taxation."

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8. McCulloch v. Maryland (1819), 4 Wheat. 316. See the remarks of Duff J. in A.G.B.C. v. A.G. Canada (1922), 64 S.C.R. 377 at 385.

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3. Outline of Contents

The major unresolved problems in the distribution of taxation powers in Canada concern primarily provincial powers. Accordingly, the major share of attention is devoted to considerations of provincial taxing competence. Chapter 2 examines certain problems relating to gaps in the federal taxing power. Chapter 3 considers the scope of provincial taxing powers at the present day. This is analyzed first from the point of view of the provincial power of direct taxation within the province in order to the raising of a revenue for provincial purposes. Particular emphasis is given to recent jurisprudence which, as it is argued, has expanded the provincial power of direct taxation to a hitherto unknown dimension. Secondly, study is made of the provincial licensing power. This has been a constant source of difficulty in the legal literature. A new interpretation of the power is offered in light of the old cases, and is buttressed by reference to, and interpretation of, recent authority. In Chapter 4 analysis is made of the interstices in constitutional authority to tax in Canada. It is sought to identify the precise amplitude of the gaps in the constitutional distribution of powers, and their relationship to the Canadian constitutional system.

## II. DOMINION TAXING POWER

### (A) Extent of Dominion Power

The grant of taxation power to Parliament by S. 91(3) is *prima facie* plenary and absolute. No restriction appears in the text of the section, nor, absent the special cases of Sections 121 and 125, does any appear in the British North America Act. There are, however, determinate criteria of form. By Section 53 of the B.N.A. Act, all federal taxing bills must originate in the House of Commons. Section 54 provides that it is not competent to the House to adopt any taxing bill to any purpose unless the bill has first been recommended to the House by Message of the Governor General in the Session in which such Bill is proposed. Provincial Legislatures, by Section 90, are subject to like requirements in respect of provincial taxation measures.

In terms, Sections 53 and 54 contemplate significant prescriptions going to the political restraints which brake a taxing legislature. They contemplate that any Parliamentary exercise of taxation power must be signaled to the electorate loud and clear by an announcement of the event in prescribed form. The sections demand that the accountable body take clear responsbility for reaching into the taxpayers' pocket.

In fact, the sections have proved to be toothless, and for two principal reasons. First, it is by no means clear that

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Sections 53 and 54 are limitations of substance as opposed to internal rules of parliamentary procedure.[9] The distinction is important, for the latter speaks to the House of Commons alone; it is not reviewable by the Courts.[10] If the House fails to act, the law stands unchallengeable. Second, the sections fall within the amending power of Parliament.[11] Even if the sections permit judicial review, "nothing prevents Parliament from indirectly amending SS. 53 and 54 by providing for the levy and appropriation of taxes in such manner as it sees fit, by delegation or otherwise."[12] Accordingly, it may well be that Parliamentary failure to observe the terms of the sections, without more, is sufficient to constitute an implied amendment of the sections. If this latter view be right, then the sections stand as polite requests only; they have no independent force. Since this is the view which has been adopted obiter by a majority of the Supreme Court,[13] it is unlikely that Parliamentary failure to comply with sections will result in constitutional defect

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9. This issue by considered, but found unnecessary to resolve by Laskin J. in Reference re Agricultural Products Marketing Act, S.C.C. Jan. 19/78, pp. 25-7

10. Conklin, Pickin and Its Applicability to Canada, (1975), 25 U. of T. L.J. 193; Swinton, Challenging the Validity of an Act of Parliament: the Effect of Enrolment and Parliamentary Privilege, (1976), 14 O.H.L.J. 345.

11. B.N.A. Act, S. 91(1).

12. Reference re Agricultural Products Marketing Act, (1978) 19 W.R. 361, per Pigeon J. at 367.

13. Id.

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on a court challenge.

B. RESTRICTIONS ON FEDERAL TAXING COMPETENCE

(1) Direct Taxation within a Province for Provincial Purposes

Although S. 91(3) prima facie grants plenary and absolute taxing competence to Parliament, the Courts have not treated it as such. The first major difficulty concerned the question as to whether the grant to the legislatures of legislative jurisdiction over direct taxation within the province in order to the raising of a revenue for provincial purposes by section 92(2) of the B.N.A. Act was an exclusive grant of power, sufficient to exclude Parliament from concurrent occupation of that field. The early method adopted by the Privy Council for interpretation of the B.N.A. Act[14] appeared to dictate an affirmative answer. In Bank of Toronto

14. Citizen's Insurance Co. v. Parsons (1881-2, 7 App. Cas. 96 at 109:

> "...The two sections [of the B.N.A. Act] must be read together, and the language of one interpreted, and, where necessary, modified by, that of the other."
>
> "Notwithstanding this endeavour to give pre-eminence to the dominion parliament in cases of a conflict of powers, it is obvious that in some cases where this apparent conflict exists, the legislature could not have intended that the powers exclusively assigned to the provincial legislatures should be absorbed in those given to the dominion parliament. ...So the raising of money by any mode or system of taxation, is enumerated among the classes of subjects in Sec. 91 but though the description is sufficiently large and general to include direct taxation within the province in order to the raising of a revenue for provincial purposes, assigned to the provincial legislatures by Sec. 92, it obviously could not have been intended that, in this instance also, the general power should override the particular one."

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v. Lambe[15] Lord Hobhouse suggested that Parliament acquired no concurrent power in respect of direct taxation within the province for provincial purposes. This view was confirmed subsequently in Caron v. The King.[16] The result is that S. 92(2) is treated as being carved out of S. 91(3), leaving behind an area of federal incompetence.

(2) Indirect Taxation Within A Province for Provincial Purposes

That there was any area of federal disability raised the further question as to whether Parliament is competent to raise revenue for provincial purposes by indirect taxation. The view has been expressed[17] that this is a provincial power only, and there are judicial dicta to that effect.[18] Chief Justice Laskin, writing as a law professor, noted that "having regard to developed constitutional

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14.cont'd. Russell v. The Queen (1881-2), 7 App. Cas. 829: "According to the principle of construction... the first question to be determined is whether the Act now in question falls within any of the classes enumerated in Sect. 92, and assigned exclusively to the legislatures of the Provinces. If it does, then the further question would arise, viz. whether the subject of the Act does not also fall within one of the enumerated classes of subjects in Sect. 91, and so does not still belong to the Dominion Parliament;" at 836-7.

15. Bank of Toronto v. Lambe (1887), 12 App. Cas. 575.

16. Caron v. The King [1924] A.C. 999

17. Kennedy and Wells, The Law of the Taxing Power (1931), p. 152.

18. Caron v. The King [1924] A.C. 999.

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principles in respect of revenue or taxing measures (principles emphasized by ss. 54 and 90 of the B.N.A. Act), it is odd indeed that governmental initiative (if not responsibility) for the raising of revenue for provincial purposes should be exercised by the federal ministry." [19] That view recites as constitutional principle a precept of politics which many Canadian Prime Ministers have uttered respectfully. Sir Wilfred Laurier put the point this way:

> "It is a sound principle of finance, and still sounder principle of government, that those who have the duty of expending the revenue of a country should also be saddled with the responsibility of levying it and providing it. (20)
>
> ....
>
> The principle by which one government collects the revenues and another government spends them is wholly false." (21)

On the other side of the balance, the following points should be noted. There is no restriction in the B.N.A. Act that Parliament confine itself to raising moneys for federal purposes. In any event a rigid distinction between federal and provincial purposes going to constitutional incompetence is more than a little strange. How can it ever be said conclusively that expenditure for a province is not also expenditure for the nation? The education of Quebec citizens, for example, is also the education of Canadian citizens and thereby serves of necessity twin and complementary

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19. Laskin, Canadian Constitutional Law (4th rev. ed.), p. 703.

20. As cited in Huggett, Tax Base Harmonization and Alternatives, 1977 (Toronto:Ontario Economic Council, 1977), p. 55.

21. As cited by Premier Maurice Duplessis, Statement to the Federal Provincial Conference, Oct., 1955 repr. in The Financing of Canadian Federation, supra, Appendix B, p. 121, Rt. Hon. MacKenzie King described separation of taxing and spending authority as "a bad system, a thoroughly vicious system;" Ibid.

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purposes. Moreover, the plain wording of S. 92(2) withholds this power from the legislature by disentitling them from imposing any indirect taxation. If the legislatures are incompetent to the task, it seems hard to think that Parliament is similarly disabled. That would leave a power vacuum in the constitution.

At first blush, it seems unlikely that Parliament would attempt to raise moneys for purely provincial purposes. Certain delegation schemes, however, bring this problem into stark relief. A pertinent example of such a scheme is accomplished by the Agricultural Products Marketing Act [22] which, as part of a comprehensive egg marketing regulation, authorizes a provincial board to collect indirect imposts for provincial purposes. The Act recently has been the subject of a major constitutional battle.[23] In considering Parliament's competence to levy indirect taxation for provincial purposes Mr. Justice McKinnon, in the Court of Appeal, "with some hesitation" held the indirect levies a valid exercise of

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22. The Agricultural Products Marketing Act R.S.C. 1970, c.A-7.

23. Reference re The Agricultural Products Marketing Act, (1978), 19 N.R. 361 (S.C.C.).

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Parliamentary authority.[24] That affirmative holding was pushed back into uncertainty by the Supreme Court of Canada which, in holding that the levies in question did not amount to taxation, found it unnecessary to decide the instant point. Chief Justice Laskin said this:

> "The distribution of taxing authority suggests another limitation, this being a limitation on federal power to impose indirect taxation for provincial purposes. The question, as is well known, was raised and left open in Caron v. The King [1924] A.C. 999 at p. 1004 by Lord Phillimore and I leave it open here. There is, nonetheless, some incongruity in Parliament legislating to impose or authorize taxation for provincial purposes but that may be an undue nod to excessive formality."[25]

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24. The reasoning of Mr. Justice MacKinnon is of some interest. He said this:

> "The principle that the British North American Act has exhaustively distributed legislative power, with some limitations not irrelevant, between Parliament and the Legislature, means that if the Provinces do not have the power to tax indirectly for Provincial purposes then Parliament must have that Power. The one exception called out of the general federal taxing power as noted by Sir Montague Smith in the Citizen's Insurance Company of Canada v. Parsons (1881), 7 A.C. 100 at 108 is 'direct taxation within the Province, in order to the raising of a revenue for Provincial purposes'. It is clear that Parliament in carrying out its national obligations, can make grants to individual Provinces and raise money by general taxation for such purposes.
>
> Its power to impose indirect taxes for any purposes is unlimited by the constitutional Act. In light of the authorities and the legislative history of the legislation, particularly its enactment immediately following the reaffirmation of the Crystal Dairy characterization of equalization levies in reference re: the Farm Products Marketing Act, and the fact that both the Province and Canada support the legislation, I am of the opinion that section 2 (through) is not colourable legislation but is bona fide competent legislation in relation to indirect taxation," (sic.); Reference re Agricultural Products Marketing Act, (1977), 78 D.L.R. (3d) 477 at 495.

25. Reference re Agricultural Products Marketing Act (1978) 19 N.R. 361 at 400-1.

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The Agricultural Products Marketing Act Reference boldly highlights the difficulty posed by a ruling that would disentitle Parliament to levy indirect taxation for provincial purposes. By creating a power vacuum in the constitution, certain forms of federal-provincial co-operation, desirable, arguendo, on all rational grounds of policy become impossible. Suppose, for example, that the levies considered in the Reference had been found to constitute taxation as had been the case with similar levies in an earlier Privy Council appeal.(26) In that hypothetical event, a 45 year old attempt to find a suitable formula for marketing agricultural products would have come to a catastrophic nothing; the attempt by each legislature acting alone would have failed and the attempt at co-operative action between the central and provincial governments acting in concert would have failed likewise. No solution to a vital

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24. cont'd There is an obvious policy component to this decision and that is this: Parliament acted upon the advice of the Supreme Court in 1957 in amending the Agricultural Products Marketing Act. [Mr. Robinette, counsel for CEMA, forcefully made this point in seeking to support the legislation in argument before the Supreme Court.] Pursuant to the amendment the Canadian egg marketing agency collected some 13 million dollars in levies. It is a co-operative marketing scheme supported by the Provinces and the federal government. Certainly any Court would be slow to interfere in such a scheme and would lean to support it.

26. Lower Mainland Dairy Products Sales Adjustment Committee v. Crystal Dairy Ltd. [1933] A.C. 168.

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Canadian problem would have lain plainly in view. The more such power vacuums litter the constitution, the more difficult does co-operative federalism become, and the more like a straight-jacket than a blueprint for effective government do constitutional restraints appear. Absent compelling reasons of policy or human rights, power vacuums should be avoided. In my view, the suggestion that the enacting legislature must be seen to be assuming responsibility for its taxation measures has limits, and those limits are reached when the principle threatens constitutional flexibility. That would be the situation were a court to prohibit Parliament from levying or authorizing such taxation. In my submission it ought not to be done by any court.

(3) Limits of Federal Spending Power

The Dominion government has a plenary authority to spend or gift any moneys in its possession as it sees fit. Section 91(1A) of the B.N.A. Act, The Public Debt and Property, is the constitutional source of such authority.(27) If Parliament makes gifts it

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27. Trudeau, Federal-Provincial Grants and the Spending Power of Parliament (Ottawa: Queen's Printer, 1969), p. 12. Professor Driedger has taken exception to this point in conversation. He suggests that the source of the power is section 102, which provides:

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27.. cont'd.

> "All Duties and Revenues, over which the Legislatures of Canada, Nova Scotia, and New Brunswick before and at the Union had and have Power of Appropriation, except such portions thereof as are by this Act reserved to the respective legislatures of the Provinces, or are raised by them in accordance with the special Powers conferred on them by this Act, shall form one Consolidated Revenue Fund to be appropriated for the Public Service of Canada in the Manner and subject to the Changes in this Act provided."

With respect, my difficulty with Professor Driedger's position stems from the words "the Public Service of Canada". "Public Service", to my mind, contemplates the civil service; it does not embrace capital improvements. Moreover, even if it did, the limitation to "Canada" appears to exclude appropriation purely for provincial purposes. This would be a significant restriction. For example, it would, in terms, restrict disaster funds following a natural calamity.

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may attach whatever conditions it desires to such gifts.(28) It can, by means of conditional gifts, make it exceedingly tempting for a province to follow a particular course of action. There is no constitutional objection to a gift to a provincial legislature, for example, of "$1 million per annum, but if it happens that 70 per cent of the provinces' students fail to pass certain health requirements set out hereinafter, the gift is to terminate." No province is obliged to accept such a gift.(29)

Intergovernmental conditional transfers are of great, albeit declining importance in Canadian federalism. In fiscal 1976-77 total conditional transfers to the provinces in the form of shared cost programs totalled 7.35 million dollars; estimated figures for 1977-78 reveal a figure of 5.61 billion dollars.(30)

Although the Dominion has a wide latitude to raise moneys by taxation, and an equally wide latitude to spend moneys thereby

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28. Scott, The Constitutional Background of the Taxation Agreements (1955), 2 McG. L.J. 1 at 6. Professor Scott makes the point that the source of Parliament's power to make conditional gifts is the royal perogative and the common law.

29. Reference re Employment and Social Insurance Act [1936] S.C.R. 427 per Duff C.J. at 457. See generally, Smiley, Conditional Grants and Canadian Federalism (Toronto: Canadian Tax Foundation, 1963); Smiley and Burns, Canadian Federalism and the Spending Power: Is Constitutional Restriction Necessary? (1969), 17 Can. Tax J. 468; Hanssen, The Constitutionality of Conditional Grant Legislation (1966-7), 2 Man. L.J. 191.

30. Treasury Boad of Canada, How Your Tax Dollar is Spent (Ottawa: Information Canada, 1976-77, 1977-78).

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collected, it does not follow that the powers thus combined can be used to invade provincial heads of jurisdiction. There is still the requirement that the moneys raised and/or spent be "in relation to" taxation or the public debt and property, or bear a "rational functional connection" thereto.(31) Provision for the gathering together of a fund, and the spending of it, must not be "in relation to" a matter of provincial power as a colourable attempt to usurp provincial jurisdiction. This point was made forcefully by Lord Atkin in A.G. Canada v. A.G. Ont. [Unemployment Insurance Reference](32) who, in striking down the Employment and Social Insurance Act,(33) said this:

> "But assuming that the Dominion has collected by means of taxation a fund, it by no means follows that any legislation which disposes of it is necessarily within Dominion competence. It may still be legislation affecting the classes of subjects enumerated in S. 92, and, if so, would be ultra vires. In other words, Dominion legislation, even though it deals with Dominion property, may still be so framed as to invade civil rights within the Province, or encroach upon the classes of subjects which are reserved to Provincial competence."(34)

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31. Papp v. Papp [1970] 1 O.R. 331 (C.A.) per Laskin J.A.,
32. A.G. Canada v. A.G. Ont. [1937] A.C. 355.
33. Employment and Social Insurance Act S.C. 1935, c. 38.
34. [1937] A.C. 355 at 366-7. See also In Re Insurance Act of Canada [1932] A.C. 41 where at 52-3 Viscount Dunedin said this: "Now as to the power of the Dominion Parliament to impose taxation, there is no doubt. But if the tax as imposed is linked up with an object which is illegal the tax for that purpose must fall."

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All taxation ultimately involves regulation; "to some extent it [taxation] interposes an economic impediment to the activity taxed as compared with others not taxed."(35) Lord Atkin's often repeated statement draws attention to that fact; it underlines that there must be a dividing line between regulatory effects, created by taxation, which are tolerable, and regulatory effects which are not tolerable.

What is that dividing line? Ultimately that question falls to be decided here: if a taxing statute effects, in addition to taxation, clearly discernible regulatory results, the validity of the statute depends on whether the subject matter of the regulation falls within, or is necessarily incidental to, the regulatory powers of the jurisdiction levying the tax. If it does the taxing statute stands unimpeded; if it does not, the taxing statute is as incompetent to the jurisdiction as is the exercise of the regulatory power simpliciter. This point, gleaned from American, Canadian and Australian cases, was succinctly put by Professor MacKinnon in 1964:(36)

> "In other words, where a statute both taxes and regulates, its validity as a whole depends on whether the taxing authority has power to regulate the subject matter affected by the tax, and it is immaterial whether the tax is inoperative in respect of those who comply with the statute's regulations. The tax is in aid of

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35. Sonzinsky v. United States (1937), 300 U.S. 506 at 513.

36. MacKinnon, Comparative Federalism (1964), p. 99.

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> the regulation; if the regulation be valid, then so also is the tax; if the regulation be invalid, the tax is invalid also."

The spending power draws attention to a rather nice question. Suppose Parliament raises moneys by taxation, and launders those moneys through the Consolidated Revenue Fund. It proceeds to return the moneys to the provinces in the form of conditional grants directed to purposes under provincial jurisdiction. Is the prohibition in the Unemployment Insurance Reference thereby activated? It seems hard to believe that this means of subverting federated jurisdiction would be tolerated were Hansard to disclose this intention in relation to the scheme as a whole. Yet the question remains as to how far conditional grants need go before they are viewed as a device subversive of confederation. Mr. Chief Justice Laskin has suggested that perhaps Lord Atkin, in the Unemployment Insurance Reference, went too far.[37] It is decidedly worth considering whether, on the contrary, he did not go far enough.

Objections to federal use of the spending power have been confined to the political and administrative levels; Canada's eleven governments have exhibited a clear reluctance to test the reach of the federal spending power by a court challenge. Nevertheless, intergovernmental transfers ultimately are subject to

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37. Laskin, op. cit., f.n. 19, p. 638.

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constitutional constraints. These cannot be fully appreciated without consideration of the policy issues involved.

At the outer limit of the spending power three heads of policy emerge: (1) Intergovernmental transfers blur electoral lines of responsibility. The electorate is confused as to which governmental body is responsible for what policy. Electoral accountability is diminished. (2) Intergovernmental transfers interfere with the decision making process of the recipient government. [This objection is limited to conditional transfers only.] The donnee government finds it unacceptably difficult to refuse the conditional grants as it thereby subjects its electorate to taxation without benefit. The recipient government loses motive power in initiating programs. Its priorities are altered. (3) Interprovincial transfers [limited to conditional transfers] allow the donor government to formulate policy in areas of jurisdiction incompetent to it and exclusively competent to the donnee government. The transfers become a means of making watertight federated jurisdictions permeable to action by the incompetent government. They disturb the constitutional division of powers.[38]

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38. These objections are considered generally in Trudeau, Federal Provincial Grants and the Spending Power (Ottawa:Queen's Printer, 1969), pp. 16-18; Clark, Fiscal Need and Revenue Equalization Grants (Toronto: Canada Tax Foundation, 1969), pp. 9-13.

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These objections are undoubtedly weighty, but they gather no strength in a vacuum. They must be tested against the constitutional design of a federal state, and the federal purposes that are nourished by the challenged procedure. Absent specific constitutional prohibition, allegations of implicitly obnoxious constitutional effects must be balanced against the special requirements of divided jurisdiction.

Intergovernmental transfers further three major policies: (1) The transfers assure a minimum acceptable level of public services in different regions. This responds to the perceived consensus of the national constituency and to the inherent purpose of confederation. National economic policies, such as the tariff, artificially force the economic growth of certain regions, intergovernmental transfers redress the balance by redistributing the benefits of federated union. The point has been succinctly summarized by Mr. Lynn:

> "Some difference between service levels between regions in a federal state are acceptable as a logical consequence of the autonomy enjoyed by the regional governments, but if the differences become intolerable to those in the lower income regions, the federation may dissolve." (39)

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39. Lynn, Federal-provincial Fiscal Relations supra, p. 15.

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(2) Public investment involves certain spillover effects which result from the lack of congruence between provincial jurisdictions and tax cost/benefit areas.(40) When spillovers become great, as when the province paying for the program benefits, in a relatively large way, those who are not members of the tax region, provincial reluctance to undertake the program is considerable. To take the obvious example, if a province discovers that the graduates of a particular costly education program consistently migrate to other provinces it will shrink from footing the bill for providing that particular educational opportunity. "In other words, underspending on services will result if a community is aware that some benefits generated by its spending spillover to individuals outside... The up shot is simply that some important public services will be undersupplied from the viewpoint of society as a whole.(41) Only a government responding to a national constituency can compensate, constitutionally and politically, for regional spillover effects.

(3) An integrated common market, such as Canada strives to be, requires a high degree of mobility for labour and capital. If the quality of important social services and benefits differs sharply across different

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40. See generally: Oates, The Theory of Public Finance in a Federal System (1968), Can. J. of Econ. 51-2; Carter, Canadian Conditional Grants since World War II (Toronto: Canada Tax Foundation, 1971) pp. 11-20; Young, Federal Provincial Grants and Equalization, in Issues and Alternatives, 1977 (Toronto: Ontario Economic Council 1977) p. 41.

41. Carter, Canadian Conditional Grants since World War II (Toronto: Canadian Tax Foundation, 1971), p. 12.

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regions of the federation, an impermissible chill to mobility may be generated. Inefficient or lopsided economic development may result. Federal responsibility for the national economy and for the inherent rights of citizenship demands federal attention to such effects.

In the event a constitutional challenge is made to the machinery of conditional intergovernmental transfers, it is highly dubious that a per se ruling - the grants are or are not permissible per se - would be warranted. The specific grant in question should fall to be tested upon the policies outlined above and upon whatever additional constitutional support it obtains from the catalogue of constitutional powers to which it relates. It is clear that the use of taxation power alone to amass funds does not validate any subsequent use of those funds.[42] But the precise range of objects and effects, and their mechanisms, to which the constitution permits intergovernmental transfers to be address is not at present precisely discernible. It is a delicate matter of constutional policy, to be worked out in the circumstances of each particular case, on a case by case basis, if judicial clarification should be sought. Narrow judicial rulings on highly charged political issues encourage compromise;

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42. A.G. Canada v. A.G. Ont. [Unemployment Insurance Reference] [1937] A.C. 355 at 366-7.

if political compromise or restraint is not forthcoming, the court inevitably will have a second opportunity to consider the issue, and this with greater experience of the effects judicial intervention has produced.

(4) Taxation of Provincial Consolidated Revenue Fund

Section 126 of the B.N.A. Act reserves to the provincial legislatures control of the provincial Consolidated Revenue Fund to be appropriated for the Public Service of the province. S. 125 additionally, in terms prohibits taxation of property belonging to any province. It is difficult to see that the Consolidated Revenue Fund is not property belonging to the province. Parliament, thus, is disentitled from imposing on the provincial fund.

(5) Double Taxation Unobjectionable

It is clear law that no objection can be taken to a Dominion taxing statute on the ground that it, in harness with a provincial impost, constitutes double taxation.(43) If the taxpayer's assets are insufficient to satisfy both levies, the Dominion and provincial claims rank pari-passu.(44) By the paramountcy doctrine, the Dominion is competent to provide that, in the case of insufficiency, its claims shall be satisfied first.(45)

43. Forbes v. A.G. Manitoba [1937] A.C. 260.

44. In re Silver Brothers [1932] A.C. 514.

45. Re R.A. Nelson Construction (1965), 52 D.L.R. (2d) 189.

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## III. PROVINCIAL TAXING POWERS

### A. DIRECT TAXATION

The constitutional division of expenditure authority in Canada has remained largely unchanged since confederation. The provincial governments still are responsible for such areas as education, health, welfare and other forms of social assistance, asylums, administration of justice in the province, local public works and municipalities. What has changed, and changed radically since 1867, is the substance of political economy and consensus respecting what is the proper role of government in discharging responsibility for precisely these areas of jurisdiction. In 1867, in accordance with laissez faire economics, provincial expenditures in the above fields were negligible. The complete opposite is the case today. There is active and expanding governmental initiative in all provincial areas of jurisdiction noted. The amounts account for the vast bulk of public expenditure. Very considerable sums, oftentimes half of the total expended, are recouped by the provincial governments from the federal government in the form of conditional and unconditional transfers. In fiscal 1976-77 such transfers totalled over ten billion dollars. Certain figures are particularly revealing. In

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1976-77 total federal conditional grants to the provinces in respect of hospital insurance amounted to 2.8 billion; medicare amounted to .95 billion; post secondary education amounted to 1.5 billion; other health and welfare amounted to 52 million.(46) The University of Ottawa, for example, which is one of fifteen provincially supported universities in Ontario, has an annual operating budget in excess of $65 million. Half of this sum is recouped by means of grants from the federal government. The balance comes largely from the provincial treasury, which must be filled by means of provincial taxation. Of course, all of this would be impossible by the original inspiration, in respect of taxing and spending authority, of the B.N.A. Act.

In fact, the constitutional distribution of taxation powers proved unworkable from the start. The provinces found themselves without sufficient revenues to discharge their limited functions. More, the transfer of revenues and responsibilities following confederation, put all provinces in a deficit position.(47) When the Privy Council's interpretation of the B.N.A. Act enormously increased provincial jurisdiction, some means had to be found to finance expanding provincial responsibilities.

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46. Treasury Board of Canada, How Your Tax Dollar is Spent (Ottawa: Information Canada, 1976-7).

47. Lynn, Federal-Provincial Fiscal Relations, supra, p. 48.

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Three mechanisms were tried to ameliorate the unsatisfactory constitutional arrangement: (1) Dissolution of the confederation. This was not conspicuously successful. Nova Scotia was the only government to attempt it. Within two years from the union, under the leadership of Joseph Howe, the Imperial Parliament was petitioned to release the province from confederation. (2) Increase in the subsidies paid under the B.N.A. Act. Despite some early federal willingness to alter the subsidies stated by the B.N.A. Act to be in full settlement of all claims on the central government, several events intervened to make the dominion government rely on the full settlement clause and refuse further increase. A global depression, beginning in 1873, place a severe crimp in the central government's fiscal capacities. The railroads entailed vast expense, creating further federal monetary restraint. From 1873 until 1907 the subsidy payments stood unaltered. (3) Resort by the provinces to their own powers of taxation. Some means had to be developed to make these significant. The means found was a judicial stretching of the concept "direct taxation" to encompass modes of taxation which would have been quite unimaginable to the Fathers of Confederation.

(1) The Legal Test

The terms "direct and indirect taxation" were first considered by the Privy Council in A.G. Quebec v. Reed.[48] In

48. A.G. Quebec v. Reed (1884) 10 App. Cas. 181.

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that case the Earl of Selbourne L.C. took as the measure of these words, their use in Mill's Principles of Political Economy. Mill had said this:(49)

> "Taxes are either direct or indirect. A direct tax is one which is demanded from the very person who it is intended or desired should pay it. Indirect taxes are those which are demanded from one person in expectation and intention that he shall indemnify himself at the expense of another; such are the excise or customs.
>
> The producer or importer of a commodity is called upon to levy a tax on it not with the intention to levy a peculiar contribution on him, but to tax through him the consumers of the commodity, from whom it is supposed that he will recover the amount by means of an advance in price."

In Bank of Toronto v. Lambe(50) a Quebec statute imposed a tax on every bank doing business in the province varying with the paid-up capital of the bank. Lord Hobhouse, in considering the validity of the tax, applied Mill's test, but vastly changed the meaning and scope of the words used. First, it was said that the test was a legal and not an economic one; accordingly, the opinions of economists as to the ultimate incidence of the tax were of no relevance. Second, the question was what did the words mean as used in the statute. The Court has to determine, accordingly, the general tendency of the tax and the common understanding of men as

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49. Mill, Principles of Political Economy (1893 ed.) Bk.V, c.3.

50. Bank of Toronto v. Lambe (1887), 12 App. Cas. 575.

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to those tendencies.

The general tendency of a tax is a question of substance and not of form; it does not depend on the particular words used in the statute. The ultimate incidence of the tax in any particular case is not of significance in determining the legal validity of the tax within Lord Hobhouse's test.(51)

It is very fine to distinguish general tendency from ultimate incidence. But the question has to be put squarely as to what meaning, if any, the concept "general tendency as commonly understood" has. In Lambe's case there could be no question that the taxation would work its way through the bank's operations and be passed on to the bank's customers in the form of increased charges for services. Does the test mean, therefore, that the Court should pretend a total lack of sophistication in appreciating this?

A lot of learning can go into distinguishing direct and indirect taxation. But how useful is it? The original rationale for the distinction was that the provinces should be prevented from embarking on ambitious expenditures. It was thought the best

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51. Halifax v. Fairbanks Estate [1928] A.C. 117, A.G.B.C. v. Kingcome Navigation Co. [1934] A.C. 51, Charlottetown v. Foundation Maritime Co. [1932] S.C.R. 589.

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way to do this was by subjecting the legislatures to the political resistance encountered in levying direct taxation. By archiaic political economy direct taxation was thought to be more perceived. It provided, therefore, for greater scrutiny of the actions of the legislature by the electorate.(52)

No one now seriously believes that the provinces do not have very significant and expensive responsibilities. Nor does anyone seriously contend that direct taxation has any more or less advantages than indirect taxation from the viewpoint of political economy. A crucial question, to which I shall return, must be put: what purpose does the distinction between direct and indirect taxation serve at the present day and what constitutional value does it protect?

(2) Collateral Indirectness

By Mill's political economy any indirectness in a taxing statute was in and of itself invidious as tending to obfuscate the actions of the legislature. If any indirectness whatever is a stigma going to provincial legislative incompetence, complex forms of provincial taxation must give the courts some considerable difficulty. Further, hybrid forms of taxation specifically must be incompetent to provincial legislatures, insofar as the hybrid

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52. CIGOL v. Saskatchewan (1978), 80 D.L.R. (3d) 449 (S.C.C.).

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partakes of a measure of indirectness.

One of the more positive developments in recent jurisprudence has been the toleration by the courts, and indeed the explicit condoning, of ancillary or collateral features of indirectness in a taxing statute. This is very important in that most forms of taxation leading to constitutional attack today are hybrid forms. They are forms which were unknown in 1867 or in the early years of the present century.

The judicial tendency to uphold provincial powers of collateral indirect taxation is observable in several recent cases. Re Minister of Finance of British Columbia v. Pacific Petroleums Ltd.(53) involved the validity of the Coloured Gasoline Act,(54) which imposed a tax on every purchaser of coloured gasoline. A "purchaser" was defined as "any person who within the province purchases gasoline when sold for the first time". The definition of purchaser was subsequently amended retroactively. It defined a purchaser as one who "purchases or received delivery of gasoline for his own use or consumption or for the use or consumption by other persons at his expense or on

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53. Re Minister of Finance of B.C. and Pacific Petroleums Ltd. (1977), 71 D.L.R. (3d) 404.

54. The Coloured Gasoline Act, 1946 R.S.B.C. 1960, c. 63.

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behalf of, or as agent for, a principle who is acquiring the gasoline for use or consumption by the principal or by other persons at his expense." The Act was held initially invalid as imposing an indirect tax, similar to the Fuel Oil Tax Act considered by the Privy Council in A.G.B.C. v. C.P.R.,[55] but it was cured retroactively by amendment of the definition of "purchaser". Gasoline primarily for resale, as opposed to gasoline which is used or consumed by the purchaser, is not liable to taxation as such on the theory that the former situation involves a commodity tax; the latter situation involves a consumer tax only. In the course of so holding, Mr. Justice Craig said this:

> "If there were anything in the Act, from which one could infer that there was a relatively small gallonage 'resold' as opposed to 'used' within the meaning of s. 10, one could reasonably hold that the tendency of the tax was on the ultimate 'consumer' or 'user' and that, therefore, the tax was a direct tax." (56)

The crucial point to notice is that ancillary or collateral indirectness is not, in and of itself, invidious such as to invalidate the statute. A "small" measure of indirectness is competent to the provinces if in object and purpose, pith and substance, the tax is a direct tax.

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55. A.G.B.C. v. C.P.R. [1927] A.C. 934.

56. Re Minister of Finance of B.C. and Pacific Petroleums Ltd. (1977) 71 D.L.R. (3d) 404 at 410.

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By far the most important judicial pronouncements illuminating this question appear in the very recent judgment of the Supreme Court of Canada in Canadian Industrial Gas and Oil Ltd. v. Govt. of Sask.[57] The majority struck down a complex of legislation which had the effect of freezing the profits from production and sale of Saskatchewan oil at pre-oil crisis levels, and bringing the excess revenues into the provincial treasury. Mr. Justice Martland saw, in the scheme an export tax, the classic form of indirect taxation, and an undue interference with interprovincial trade and commerce. But the remarks made by Mr. Justice Dickson, in dissenting reasons, respecting a different point are highly illuminating. His Lordship specifically noted that collateral indirectness was not sufficiently invidious so as to void provincial competence.

> "...taxation may well have aspects which are direct and others which are indirect. By nineteenth century political economy, any element of indirectness was a stigma as tending to obfuscate the actions of the Legislature. That consideration is of minor importance today...More important than a vestige of indirectness is the prohibition of the imposition by a province of any tax upon citizens beyond its borders." (58)

(3) Hybrid Forms of Taxation

The realization that collateral indirectness is not in

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57. CIGOL v. Saskatchewan (1978), 80 D.L.R. (3d) 449 (S.C.C.).

58. Id. at 18-19.

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itself disabling to a province turns a spotlight on hybrid forms of taxation. These are the more common forms of taxation raising constitutional questions in the courts today. Examples of hybrid forms of taxation are the Oil and Gas Conservation, Stabilization and Development Act,[59] 1973, S.S. 1973-74 as amended by S.S. 1973-74, c. 73, and the Social Services and Education Tax Act [60]

Certainly an important question, which remains unanswered notwithstanding judicial recognition of provincial powers of collateral indirect taxation, is this: how far may a province impose indirect taxation ancillary to a taxing statute which is "in relation to" direct taxation. There is a second aspect to the problem. If a hybrid statute employs no recognizable form of taxation within historically understood direct and indirect categories, how far is it competent to a province, within the meaning of Mill's test as developed by the courts, to levy collateral indirect taxation. Some answers appear from recent cases.

In Canadian Industrial Gas and Oil Limited v. Govt. of Sask. [61] the court had to consider a complex of legislation central to which was a mineral income tax. The tax was a 100% levy on the difference between the price received by production companies and the"basic well-head price", a statutory figure equal to the price

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59. Oil and Gas Conservation, Stabilization and Development Act., 1973 s.s. 1973-4 as amended by s.s. 1973-4, c. 73.

60. Social Services and Education Tax Act, R.S.N.B. 1973 c. S-10.

61. CIGOL v. Sask. (1978) 80 D.L.R. (3d) 449 (S.C.C.)

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received by the producing companies immediately prior to the phenomenal rise in price of oil by reason of the "energy crisis". In other words, the legislation sought to drain off the fortuitous profits accruing to the oil producers by reason of the energy crisis and to divert those revenues into provincial coffers. The Government of Saskatchewan, in considering whether to leave the revenues in the pockets of eastern Canadian consumers, to leave the profits in the pockets of the oil producing companies, or to appropriate the profit to itself, chose the latter. The tax was attacked as an indirect tax. The theory in support of this submission was that since the companies were prohibited from selling oil at a lesser price than prevailing world prices by reason of the tax, the levy came as a burden which would cling to the commodity and impose on extraprovincial consumers. In other words, counsel for the companies contended that the producing companies were no more than a conduit through which the Government of Saskatchewan sought to reach the consumers of eastern Canada. The Saskatchewan Court of Appeal declined to so hold. Mr. Chief Justice Culliton noted that the intent and purpose of ~~the~~ tax was obvious. The intent was to "drain off any increased return which might otherwise have come to those persons having an interest in the oil produced and sold from a well in a producing tract in Saskatchewan, as the result of any increase in the selling price after the 1st of January, 1974."[62] A minority of the Supreme

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62. CIGOL v. Sask. (1976) 65 D.L.R. (3d) 79 at 92.

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Court of Canada agreed, but the majority adopted a narrow categories approach, characterizing the legislation as an export tax and a tax on production specifically incompetent to the provinces.

The tendency to allow a measure of collateral indirect taxation in a hybrid tax situation was widened by the New Brunswick Court of Appeal in Simpson-Sears Ltd. v. Provincial Secretary of New Brunswick.(63) In that case catalogues sent into the Province of New Brunswick by Simpson-Sears Ltd. and distributed free of charge were sought to be taxed under the Social Services and Education Tax Act which levied a tax against "every consumer of goods in the Province". "Consumer" was defined as "a person who utilizes within the province goods for his own consumption or for the consumption of any other person at his expense." The word "consumption", by Section 1(d) included the word "use". At first instance(64) the tax was held indirect. Mr. Justice Barry considered that, if valid, the tax necessarily would be passed onto the final consumer or user of the catalogue if such consumer or user purchased goods from Simpson-Sears Ltd. He noted that since every person who received a catalogue is not a customer of Simpson-Sears, then, in respect of such non-customers, the transaction is complete in Ontario so far as concerns the retailer. That meant, according to Mr. Justice

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63. Simpson-Sears Ltd. v. Provincial Secretary of N.B. (1977), 71 D.L.R. (3d) 717, rev'd on other grounds (1978), 82 D.L.R. (3d) 321 (S.C.C.).

64. Simpson-Sears Ltd. v. Provincial Secretary of N.B. (1977) 14 N.B.R. (2d) 289

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Barry, that the profits in respect of that transaction would be taxation of an extra-provincial citizen, which taxation would be to that extent indirect and invalid.

The Court of Appeal reversed. Mr. Chief Justice Hughes noted that Simpson-Sears had several offices in New Brunswick and therefore was a person within the province who may be taxed if taxed directly. In order to qualify as a direct tax, "the tax must be one levied against the ultimate or final consumer or user". He went on to hold that the tax imposed by the Act on catalogues, "is not related or relatable to any unit of the commodity which the company advertises and sells and cannot be regarded as a tax which clings as a burden to a unit of the commodity or its price or to the transaction presented to the Market". The tax qualified as a consumption and use tax and it was therefore irrelevant that the company may be able to shift the burden of the tax to purchasers of its merchandize. There was, he said, no question as to taxation of an extra-provincial citizen. "Although the company has its head office in Ontario, it has several places of business within New Brunswick and is therefore a person who may be taxed here, if taxed directly..." (65)

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65. Simpson-Sears Ltd. v. Prov. Secretary of N.B. (1977) 71 D.L.R. (3d) 717 at 723.

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Further appeal to the Supreme Court[66] produced inconclusive results on the constitutional issue. The Court split 4 - 4. Chief Justice Laskin, the ninth voice, contented himself with allowing the appeal on the basis that proper construction of the New Brunswick statute failed to bring Simpson-Sears within its ambit; he left the constitutional question open.

Taxation of promotional materials - that is the essence of the Simpson Sears dispute - does raise nice questions as to directness or indirectness. Ultimately the tax is borne by the purchaser of the promoter's goods. The retailer is in business for profit, not for fun. In that sense the tax is indirect in that the legislature taxes the consumer, through the retailer, in the form of an increase in the price of the goods. Even unsophisticated evidence will reveal this; in fact, such evidence formed the foundation of Mr. Justice Ritchie's reasoning in holding the statute constitutionally defective for want of compliance with the directness requirement.

However, this aspect - the ultimate incidence of the taxation - is precisely what the Courts ever since Bank of Toronto v. Lambe[67] have refused to regard as determinative. Evidence

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66. Simpson Sears Ltd. v. Provincial Secretary of N.B. (1978), 18 N.R. 590; 82 D.L.R. (3d) 321 (S.C.C.)

67. Bank of Toronto v. Lambe (1887) 12 App. Cas. 575.

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that the ultimate incidence of the tax is passed on is irrelevant; there is weighty authority that such evidence is not even admissible.(68) Bank of Toronto v. Lambe is itself the locus classicus of this rule and the perfect example. That case involved consideration of a tax on the paid up capital of the bank. The Bank, like Simpson Sears, is also in business for profit, and not for fun. It, too, passed on the tax to its customers in the form of increased charges for services. But the tax does not thereby become indirect. The test is not the ultimate incidence; it is the "general tendency as commonly understood."

The lack of judicial accord in these cases is startling. There is no agreement in the Supreme Court and the limit is reached in the number of successful appeals. This suggests an uncertain and unstable state of law. There is a certain inevitability about this in the hybrid tax situation. Although the courts are prepared to accept small quantums of indirectness collateral to a direct taxation statute, hybrid taxes present them with intractable puzzles. The difficulties in applying Mill's test as developed by the courts are in any case formidable; hybrid taxation increases the complexity and leads to judicially erratic results. Not one of these cases is free in each court from a statement by a judge that the question for consideration is "difficult".

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68. Cairns Construction v. Government of Saskatchewan [1960] S.C.R. 619 aff'g 16 O.L.R. (2d) 465.

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Hybrid forms of taxation inevitably produce judicially erratic results. The courts appear prepared to accept small amounts of indirectness, but the difficulties encountered in applying Mill's test as developed by the courts very quickly makes judicial conclusions difficult to predict. This is especially exaggerated in the case of hybrid taxation.

Drafting technique can help. However, it would be wrong to think that the draftsman should concentrate his major energies on the directness requirement. That is precisely where the courts will lean to assist him if he strays from the straight and narrow and produces collateral indirect results. The prudent draftsman should insure that he has a firm basis of jurisdiction "within the province". The jurisdiction must fasten on persons, property or transactions located within the provincial jurisdiction and the draftsman should take pains that the statute does so plainly. If the statute produces collateral indirect effects, the draftsman must make obvious that these do not travel beyond the provincial borders. The basis of jurisdiction to which the statute attaches cannot be used as a conduit to reach extra provincial citizens. The statute must be drafted such that the tendency and the incidence of the taxation <u>both</u> do not overstep the provincial territory and clearly can be seen not to do so, for, if it does, the draftsman will find little aid forthcoming from the courts. This tendency emerges from all of the recent case law,

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and it is specifically referred to by the minority of the Supreme Court in the CIGOL appeal. In short, collateral indirectness, either ancillary to a direct taxation statute or as part of the effect of a hybrid statute, will be tolerated if the effect is relatively small and localized to the province. It seriously jeopardizes the entire statute when the incidence of taxation plainly reaches extra provincial residents, or when, in a hybrid statute, the incidence cannot plainly be seen to impose locally exclusively.

(4) Commodity and Consumer Taxes Distinguished

(i) Basis of the Distinction

One of the most important ways in which the concept of direct taxation has been stretched to flatter provincial competence is by the introduction of a distinction between commodity taxes and consumer taxes. A commodity tax as a category per se is indirect.(69) Mill himself said so.(70) He noted that a commodity tax was a means of building into the price of a commodity an impost and through the producer of the commodity to send that impost abroad to the purchaser of the commodity. Mill thought such was the classic form of indirect taxation.

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69. A.G.B.C. v. C.P.R. [1927] A.C. 934; A.G.B.C. v. McDonald Murphy Lumber Co. [1930] A.C. 357.

70. Mill, Principles of Political Economy (1893 edition) II, p. 435.

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A consumer tax is very much like a commodity tax in its mode of operation but the intention is very different. It is an intention to tax the last purchaser, the consumer, only. Accordingly, there can be no passing on of the tax. Consumer taxes are held by the courts to be direct.(71)

The distinction between commodity and consumer taxes is necessitated by the need to escape from the straight-jacket of Mill's archiaic political economy. A commodity tax, if given its head as a category incompetent to the provinces per se, is capable of voiding any attempt to tax a transaction where a subsequent sale may be anticipated.(72)

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71. Atlantic Smoke Shops v. Conlon [1934] A.C. 550; Cairns Construction v. Government of Saskatchewan [1960] S.C.R. 619. Mr. LaForest, The Allocation of Taxing Power under the Canadian Constitution (Canadian Tax Foundation, 1967) is of the view that the categories test elaborated by the Privy Council in Halifax v. Fairbanks [1928] A.C. 117 is a departure from Mill's theory, an errant judicial innovation in an otherwise orderly progression: pp. 70-3. It follows from the above that I am in disagreement with this view. I consider that the categories test was an intensified application of Mill's theories. It stretched his arcane political economy to the breaking point. Mr. LaForest thinks the categories test is not dead [p. 72]; in my view it is so, at least insofar as new forms of taxation are concerned. Such forms are almost always hybrids. No worthwhile analysis attempting to be faithful to searching methods of constitutional scrutiny, would employ such an unsophisticated device in respect of hybrid taxes.

72. In A.G.B.C. v. C.P.R. [1927] A.C. 934, Viscount Haldane voided the Fuel Oil Tax Act R.S.B.C. 1924, c. 251 on the theory that as fuel oil is a marketable commodity,"Those who purchase it acquire the right to take it into the market. It therefore comes within the general principle which determines that the tax is an indirect one;"at 938.

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The commodity-consumer tax distinction first received judicial elaboration in Atlantic Smokeshops v. Conlon[73]. The Privy Council considered in that case the Tobacco Tax Act of New Brunswick. The tax imposed a 10% levy of the price paid on anyone who purchased tobacco for his own consumption from a retail vendor in the province. By regulation, the tax was to be collected by the retail vendor who was constituted a crown agent for that purpose and alloted 3% of receipts as remuneration. Viscount Simon held that, since the tax fell on the last purchaser, there could be no question of further resale; hence the tax fell on the person who actually bore the burden of it and could not be passed on. In Cairns Construction v. Govt. of Sask.[74] a tax levied on all consumers of tangible personal property at a retail sale in the province, to which was annexed the mechanism of collection by the retail vendor, was held to be direct. The facts of the case concerned the purchase by a building contractor of pre-fab housing components. Of course, in this instance, the tax would be passed on as part of the selling price of the house, but the courts had long ago said that the ultimate incidence in particular cases could not affect

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73. Atlantic Smoke Shops v. Conlon [1943] A.C. 550

74. Cairns Construction v. Government of Saskatchewan [1960] S.C.R. 619, affirming 16 D.L.R. (2d) 465, reversing 9 D.L.R. (2d) 721, noted Due, The Cairns Decision (1961), 9 Can. Tax J. 363; Baker, (1955-61) 1 Alta. L. Rev. 594.

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the validity of the tax.(75)

Finally, in A.G. Nfld. v. The Avalon Telephone Company Ltd.(76) Mr. Chief Justice Furlong considered the validity of the Social Security Assessment Act R.S. Nfld. 1952, c. 41 which required that "every purchaser shall pay to her Majesty at the time of making a purchase an assessment at the rate of 5 per centum of the purchase price of the tangible personal property purchased". A purchaser was defined to be "any person who acquires tangible personal property at a retail sale in Newfoundland for his own consumption or use or for the consumption or use by others at his expense." Mr. Chief Justice Furlong, following the lead of the Supreme Court in Cairns Construction v. Govt. of Sask.,(77) held the tax direct on the theory it was a consumer as opposed to a commodity tax. The tangible personal property referred to in the Act contemplated consumption for use and not resale. The factual situation of the litigation was that the tax was imposed on equipment purchased by a telephone company. It is inconceivable that the tax on that property would not eventually be passed on to telephone company customers in the form of increased service charges. The Newfoundland

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75. A.G.B.C. v. Kingcome Navigation Co. [1934] A.C. 45; Charlottetown v. Foundation Maritime Co. [1932] S.C.R. 589.

76. A.G. Nfld. v. The Avalon Telephone Co. Ltd. (1962), 33 D.L.R. (2d) 402.

77. Supra.

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Court thought that was not the point. The point was that indirect taxation had a cut-off point as a concept. Insofar as telephone equipment was not processed, fabricated or manufactured into the telephone services, the court would not look to the obvious pattern or route which the tax followed. The point to notice is that in the Avalon Telephone case, the court has gone beyond the theory of general tendency of the taxation which characterizes the earlier Privy Council appeals. It has artificially hived off the production and assembly of equipment from the purpose of that production and assembly -- the sale of telephone services - in order to uphold the validity of a provincial tax.

(ii) Indirect Sales Taxes for the Provinces?

These decisions have opened to the provinces the lucrative high-yield, low-rate retail sales tax, and all provinces, with the sole exception of Alberta, have entered. The taxes must observe rigid requirements of form; they must be drafted as taxes on consumption or use; they cannot validly emerge as pure indirect taxes on the retailer himself.

Many suggestions have been made that indirect sales taxes as well be opened to the provinces. In fact, constitutional amendments have been proposed and narrowly rejected to that

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effect.(78) There are several difficulties with such an amendment. First, all are agreed that the tax must be levied at the retail as opposed to the manufacturing level. The reason is that a disproportionate amount of manufacturer sales - eighty six percent in 1967-8 - occur in Ontario (fifty eight percent) and Quebec (twenty eight percent). That would unduly concentrate the benefit of the taxes in those two provinces. Retail sales taxes do not entail this problem: sixty three percent of retail sales only occur in Ontario and Quebec.(79) Additionally, manufacturers' taxes are difficult to localize. They travel throughout the country, resting ultimately on the consumer. This implies that manufacturing jurisdiction might unfairly reach taxpayers outside of their borders.

These considerations leave open the possibility of a constitutional amendment to authorize provincial indirect sales taxes at the retail level. In my view, such an amendment is unwise, and for two principal reasons. First, retail sales taxes are inherently

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78. See generally, Moore, Perry, Beach, The Financing of Canadian Confederation: The First Hundred Years (Toronto: Canadian Tax Foundation, 1966), pp. 36-7; Benson, The Taxing Powers and the Constitution of Canada (Ottawa: Queens Printer, 1969), p. 38-48, App. F; Tarasofsky, The Feasibility of a Canadian Federal Sales Tax, Studies of the Royal Commission on Taxation No. 6 (Ottawa: Queen's Printer, 1966); Due, The Provincial Sales Taxes and Their Relationship to the Federal Sales Tax (1963), 11 Can. Tax J. 523; Due, Provincial Sales Taxes (Toronto: Canada Tax Foundation, 1964), C II "The Constitutional Issues," pp. 17-34.

79. See Benson, supra, p. 42, App. D.

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regressive and unfair, they strike hardest at the lowest end of the income scale.

> "As incomes become larger, the non-discretionary element in expenditure declines as a proportion of total expenditure, so that larger incomes must bear relatively heavier taxes if the criterion of vertical equity is to be satisfied. Since sales taxes (it is assumed) are shifted forward and allocated among individuals in proportion to their consumption expenditure and since consumption tends to fall as a proportion as income rises, it is clear that sales taxes are certain to be inequitable by this criterion." (80)

This consideration lead the Royal Commission on Taxation to conclude that "rigid adherence to our equity principles would call for the complete abolition of all sales taxes. (81) Entrenchment of such an inequity in the constitution should not, in my view, be made.

Secondly, any provincial indirect sales tax would have to be founded on an agreed base or allocation formula in order to guard against the imposition, by a province, on a citizen beyond its borders. In other words, retail sales taxes are hard to confine; an allocation formula would be mandatory to insure equity and efficiency in the system. If the base be entrenched, it might well prove to be a straight jacket as the economy of the country

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80. Bird, Sales Tax and the Carter Report (Don Mills: C.C.H. Canada Ltd., 1967), p. 8.

81. Report of the Royal Commission on Taxation (Ottawa: Queen's Printer, 1967), I, 8.

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metamorphoses; if the base is not entrenched, many hazards are thereby created for jurisdictional conflict. Neither result, in my opinion, should be encouraged in a federal system.

Finally, it has never been conclusively demonstrated that change to an indirect form of sales tax possesses any significant advantages over the present form. The amendment proposals originated in the dubious validity of existing provincial imposts following the A.G.B.C. v. C.P.R.(82) and A.G.B.C. v. Kingcome Navigation Co. cases.(83) That doubt has long since been laid to rest. Greater efficiency of collection is undemonstrated, and, in fact, all evidence suggests that the present mechanism is sufficiently flexible to allow for all desirable improvements.(84) The courts have already upheld wide provincial penal powers ancillary to the Retail Sales Acts;(85) it is highly unlikely that any greater enforcement efficiency would be forthcoming under an indirect mode of imposition. Given the highly speculative nature of advantages to be gained

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82. A.G.B.C. v. C.P.R. [1927] A.C. 934.

83. A.G.B.C. v. Kingcome Navigation Co. [1933] A.C. 45.

84. Due, Provincial Sales Taxes (Toronto: Canadian Tax Foundation, 1964), pp. 31-3.

85. R. v. Christopolous (1977), 36 C.C.C. (2d) 399 (Ont.H.C.).

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by an indirect retail sales tax amendment, and the clear negative fallout, by constitutional entrenchment of inequitable taxation and creation of opportunities for federal tensions, such an amendment must be deemed unwarranted and undesirable.(86)

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86. Mr. Due's comments are instructive, Provincial Sales Taxes, supra, at p. 33-4:

> "The advantages claimed for a constitutional amendment to permit an indirect retail sales tax are thus highly illusory. The basic operation of the tax would not be changed by a shift to the indirect form, and improvements in convenience, efficiency, compliance, and cost of collection would be relatively minor. The only important advantage, the elimination of the need for separate accounting for the exact amount of tax collected, could be attained equally well under the present form of tax by allowing the retailer to keep any overage collected as compensation for his work in collection of the tax. The tax would not become hidden without drastic legislation, which would be fundamentally undesirable and would create a storm of protest if proposed.
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> On the other hand, an amendment has several disadvantages. A change in the form of the tax would complicate the application of the tax to goods bought outside the province and brought in for use, since this element would still have to be imposed on a consumer basis. As noted, any attempt to force concealment of tax would give rise to a wave of protests, and is undesirable in terms of usual principles of taxation. Furthermore, any amendment which would be politically acceptable might well be saddled with restrictions which would later prove troublesome. In 1950-51 proposed amendment limited the sales tax rate to 3%; most provinces already use a 5% figure. All in all, an amendment would not produce significant advantages, and would create substantial uncertainty and the potentiality of highly undesirable consequences."

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(5) Constitutional Litigation and the Taxing Power

The consumer-commodity tax distinction is partly based in logic - the inability of the ultimate consumer to pass on the tax - but it is more properly seen as based in constitutional policy. The court is judicially developing the concept of direct taxation in order to allow the provincial legislators wider taxing powers. This was explicitly stated by Chief Justice Furlong in the Avalon Telephone case. There is a realization by the courts that the taxation power flows from a constitutional document, and that such a document must be supple in the hands of the courts in order to provide for the needs of national life.

A constitution is not simply a statute like any other. It sets the framework of our national intercourse. It is written in broad general language capable of evolution to provide for the growth of our nation. Of course, it is impossible decisively to answer the argument, made by those hostile to judicial review, that the constitution is not limited to the original understanding of its framers.(87) It is worth noting, however, that the courts do

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87. This theory was expressed in Re Regulation and Control of Aeronautics in Canada [1932] A.C. 54.

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not treat it as such.(88) This is particularly true in the evolution of taxation powers. The Court must be guided by rigorous judicial principle certainly, but this rigour must be tempered by the sober realization that the Court is an organ of government and a political institution; "judicial review will survive only as long as the Court does not cut too sharply athwart the stream of political power, wherever the sources of that power may be found."(89) In the Avalon Telephone case Mr. Chief Justice Furlong put the point this way:

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88. Edwards v. A.G. Canada [1930] A.C. 124 at 136 ("The B.N.A. Act planted in Canada is a living tree capable of growth and expansion within its natural limits "); British Coal Corp. v. The King [1935] A.C. 500 at 518; A.G. Ont. v. A.G. Canada [1947] A.C. 127 at 154.

In Reference re Anti-Inflation Act, (1976) 68 D.L.R. (3d) 452 (S.C.C.) Chief Justice Laskin expressly negatived the view that the constitution is limited to the original understanding of its framers. He said this, at 487:

"This is not to say that clear statutes are to be unsettled, but only that the Constitution designed to serve this country in years ahead ought to be regarded as a resilient instrument capable of adaptation to changing circumstances."

Mr. Justice Dickson also has explicitly noted that it is unlikely that the "original intent" school of interpretation is appropriate for the B.N.A. Act. He said this: "...there is no reason to believe the B.N.A. Act is not a document of evolving meaning not limited to its original inspiration..." CIGOL v. Saskatchewan S.C.C. Nov. 23, 1977, p. 17.

89. Telford Taylor, Two Studies in Constitutional Interpretation (1969), p. 5.

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> "Now it has been repeated many times that law is an organic and living system by which we are enabled to conduct our day to day life in society with the minimum of disturbance. Law has to keep pace with social change - it has to operate in the society which it helped to organize, which means, in short that it has to regard the conditions of the day as they are and not as they were. This is equally true in the field of taxation. The conditions which created the definition of the many forms of taxes a century ago are in many instances no longer existing. A tax which was a direct tax 90 years ago may be an indirect tax today, and the definition of the economist may require re-statement; because the propositions of modern economics are not without the certainty of the propositions of Euclid.
> ...If virtually all taxation today is ultimately borne by the consumer of goods and services are we then expected to say that all taxation is indirect and that consequently the field for provincial taxation is almost non-existent? I think not. I think we have to see what was meant when the words were used in the Act and then see if like conditions prevail today." (90)

The Avalon Telephone case exemplifies a mature court confident of its abilities to safeguard constitutional integrity, and confident, moreover, of its ability to respond with that considered flexibility which constitutional litigation requires.

Our courts do not always act thus. They often search for received categories or certain, if outmoded, forms of analysis.

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90. A.G. Nfld. v. Avalon Tel. Co. Ltd. (1962), 33 D.L.R. (2d) 402 at 405-6.

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In Regina v. Churchill[91] the court was asked to adjudicate the validity of the Mobile Home Park Fee Act[92] which imposed a tax on "every person who is in charge of, or operated a mobile home park". Counsel argued that the tax was a novel form of taxation, unknown historically, and not, therefore, capable of assignment to any determinate form of taxation. Counsel asked the court as a consequence to apply Mill's test as developed by the Privy Council. The court declined Counsel's invitation. The mere involvement of land produced a knee-jerk reflex action in the court, who assigned it to the category of direct taxation as a tax on land. The reasoning is of interest for it indicates a theoretical rigidity; a rigidity which is not in keeping with the spirit of constitutional litigation. It is decidedly unhelpful for a court to lock itself into firm categories or determinate modes of classification incapable of evolution. That is the lesson to be gleaned from the Avalon Telephone case. The Churchill case illustrates that the lesson has been incompletely appreciated.

(6) Section 92:2 Form and Substance

(i) "Direct Taxation" a Matter of Form

Direct taxation has become an elastic concept. Many

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91. Regina v. Churchill [1972] 6 W.W.R. 107 (B.C.S.C.).

92. The Mobile Home Park Fee Act, S.B.C. 1971, c. 35.

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courts are very tolerant, absent certain prohibitions of substance, of provincial indirect taxation as a collateral matter. But there is no clear unanimity of view in the Courts. The restriction that the provinces limit themselves to direct taxation is a restriction of form only and serves no useful purpose - except as a remainder of historical ideas in political economy - at the present day.

(ii) "Within the Province" a Matter of Substance

Section 92:2, however, does contain a crucial limitation of substance. That is that provincial taxation must be "within the province". A province must found its jurisdictional competence to tax on one of three bases: it may fasten provincially located persons, property or transactions. The rules of jurisdictional competence strictly preclude any province from taxing outside its borders or from imposing on extra-provincial citizens. No province has the ability to shift its tax burden generally to the citizens of Canada or to the residents of another province. This point was very early made by the Privy Council in Bank of Toronto v. Lambe[93] and was recently underlined by a minority of the Supreme Court of Canada in the CIGOL appeal.[94] In Bank of Toronto v. Lambe,

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93. "There are obvious reasons for confining their [the legislatures] power to direct taxes and licenses, because the power of indirect taxation would be felt all over the Dominion;" (1887), 12 App. Cas. 576 at 586.

94. CIGOL v. Sask., supra.

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Lord Hobhouse suggested the limitation to tax directly was a means of keeping the burden of the taxation from falling beyond the provincial border.

(iii) Taxation of Economic Activity within the Province

There is an exception to the above limitation on the provinces. If the extra-provincial citizen is conducting economic activity within the provincial territory, the province is competent to levy taxation in respect of that activity. This was made clear by the Supreme Court of Canada in Alworth v. M.N.R.[95] That case involved consideration of the Logging Tax Act R.S.B.C. 1960, c. 225, which by s. 3(1) levied a tax as follows:

> "3(1) Every taxpayer shall for each taxation year pay a tax of 15 per centum calculated on his income derived from logging operations in British Columbia."

The court considered the essential question to be whether the tax was in personam or whether the tax was on economic activity within the province. It found that the charging section of the tax was not limited to persons who reside in the province but pointed also to a class of persons identified with the operations in respect of which the tax was imposed. The Court pointed out that it was the income derived from logging operations which carried the burden of

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95. Alworth v. Minister of Finance (1977), 76 D.L.R. (3d) 99, affirming (1977), 71 D.L.R. (3d) (B.C.C.A.).

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the tax, and not any class of persons. Therefore, as the logging activity was entirely provincial, the tax was taxation "within the province". The Chief Justice said this:

> "It would be to substitute form for substance and indeed, empty the charging section of substance (by inviting easy evasion) to hold that a personal tax is imposed by the Act."

In some respects Alworth is a simple case. It only involves determination of the question whether the tax fell on the logging operations (which are clearly within the province) or on the logger (who may be within or without the province). But a much more difficult question may arise. The court may have to determine where business income is "earned". This often is very arbitrary. There is no tested and true common law method for making this assessment. The Federal Income Tax Regulations offer definitions, (96) but they are not constitutionally obligatory. Great difficulties can arise, therefore, when two provinces provide for different ways of making this determination. Prior to the rules found today in the Income Tax Act the situation was a jungle. The Rowell Sirois Commission, in reviewing corporate taxation in 1940, described the field as inequitable, inefficient, complex, and chaotic. The

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96. Income Tax Regulations, Part IV.

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commission's solution[97] was simple - the Dominion alone should have the power to impose corporate taxes - but it was found unacceptable at the 1941 Federal-Provincial Conference, and dropped. At the Victoria Conference in 1972, the Dominion Government revived this suggestion. It proposed a renunciation, by the Provinces, of their powers to tax business incomes, in favour of the central government. At present the problem is dormant, since the provinces are in agreement on an allocation formula proposed by the Dominion.[98]

Allocation of business income, as between the various provincial jurisdictions, is a crucial problem in any federated fiscal system. Failure to reach a workable formula can result in one of three difficulties: (1) a jurisdiction might impose on profits that, by any measure, cannot be regarded as having been earned there; (2) a jurisdiction might refrain from imposing on profits rightly regarded as earned there; (3) two or more jurisdictions might impose on the same profits. Economic inefficiency and inequitable taxation would result in each case; interjurisdictional political and administrative relations would be strained. In an economic system like our own, where the most significant taxable entities straddle provincial and national borders, it is especially important that an

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97. Report of the Royal Commission on Dominion-Provincial Relations [Rowell Sirois Report) Book III, Recommendations, 114.

98. The allocation of business income system, as well as is development, is described by Smith, Allocating to Provinces the Taxable Income of Corporations: How the Federal-Provincial Allocation Rules Evolved (1976), 24 Can. Tax J. 545. Benson, The Taxing Powers and

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effective and equitable allocation formula be maintained. It goes without saying that any such formula must be tested by the demands of the constitution.

In Canada, the allocation rules have never been the subject matter of a court challenge. The applicable constitutional criteria, therefore, are entirely theoretical. But this much is clear law. Persons, including corporations, property and transactions located in a province may be taxed there if taxed directly.(99) There is no requirement that the person be domiciled or resident within the province. If a corporation carries on business there, that is a sufficient foundation upon which provincial taxing jurisdiction can fasten.(100)

It is important to distinguish upon which of the three possible foundations - persons, property or transactions - provincial jurisdiction has attached. That is a question of statutory construction: it must be discerned precisely on which of the three the statute intends to impose. That determination having been made, the question of jurisdictional competence to tax falls to be decided on

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98. cont'd. the Constitution of Canada (Ottawa:Queen's Printer, 1969) repeats the position of the Government of Canada that "the only surer way of accomplishing this objective [reaching accord on the allocation of business income] would be for the provinces to forego their power to tax business income, by agreement or constitutionally, and leave it to Parliament to levy these taxes;" at 22.

99. Bank of Toronto v. Lambe (1887), 12 App. Cas. 575.

100. Id.

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whether the basis of jurisdiction is within the province.

Jurisdictional competence to tax is an entirely different question than competence to levy a particular rate or measure of tax. Suppose, for example, that Prince Edward Island fastens its jurisdiction upon a large multi-national corporation maintaining a small retail outlet in Charlottetown. The jurisdiction clearly is well founded. The corporation is within the province. Now suppose that the measure of tax is 14% of the corporation's world wide income, and that such amount trebles the hitherto province-wide tax yield. Can constitutional objection successfully be taken against this rate?

The answer appears to be no.[101] The theory is that if jurisdiction is valid, the matter of rate poses no separate constitutional hurdle. The constraints are entirely political. If a province taxes unfairly, by this theory, the taxpayer may seek a more accomodating jurisdiction in which to carry on its activities.

To the mind of a constitutional lawyer, there is a certain unreality about this conclusion. The constitution is not such a

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101. Kerr v. Superintendent of Income Tax [1942] S.C.R. 435; C.P.R. v. Provincial Treasurer of Manitoba (1953), 4 D.L.R. 233 (Man. Q.B.).

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toothless instrument that some political fanaticism temporarily in office can try to drive out multi-national business as if ridding the world of a plague.[102] It may be that some relief could be had by the theory of a federally incorporated company's immunity to provincial laws which impair its status and essential powers.[103] But whether that doctrine be pressed into service to deal with an expanded set of problems, or whether a new judicial rule be designed, it seems extravagant to think that a total breakdown in the political arrangements as to allocation of business income will avoid constitutional scrutiny on a court test. In my submission, measure of tax, as opposed to jurisdictional competence, only awaits a proper case to be subdued by constitutional principle.[104]

Measure of tax, as a subject matter for constitutional scrutiny, turns a spotlight on the allocation rules. The Court would have to determine, ex hypothesi, the constitutional limits within

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102. See, for an illuminating example, A.G. Alberta. v. A.G. Canada [Bank Taxation Reference] [1939] A.C. 117.

103. John Deere Plow Co. v. Wharton [1915] A.C. 330; Great West Saddlery Co. v. The King [1921] 2 A.C. 91. But see Canadian Indemnity Co. v. A.G.B.C. (1976), 73 D.L.R. (3d) 11 (S.C.C.)

104. The problems involved in devising constitutional formulas respecting rate of taxation have been considered in an American context by Lowndes, Rate and Measure in Jurisdiction to Tax - Aftermath of Maxwell v. Bugbee (1936), 49 Harv. L. Rev. 756; Note, Interstate Allocation of Corporate Income for Taxing Purposes (1931), 40 Yale L.J. 1273; Powell, Business Taxes and the Federal Constitution (1925).

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which a province may attribute income to its tax base and impose on it. One can only speculate as to the result, but it does not seem illogical to suppose that the principal tests of the present allocation rules, which have been developed and refined by more than thirty years of federal-provincial consultation,[105] may acquire, by convention, a quasi-constitutional status in the event of total breakdown and resort to the courts. In that case, the courts might define broad parameters around an allocation formula based upon the proportion of gross receipts[106] and wages paid in the province (weighted 50% each) to total taxable income under the federal income tax act.[107]

One last problem remains to be considered relating to taxation of economic activity within the province. It is clear law that a province is disentitled to levy a disciminatory tax on goods

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105. Smith, Allocating to Provinces the Taxable Income of Corporations, supra, p. 568

106. By the Income Tax Regulations, S. 402(3) this amount is subject to a reasonableness test so far as concerns attribution of total revenue to the fixed place of business in the province. By S. 402(1) sales are allocated on the basis of the residence of the customer. Prior to 1957 sales were allocated on the basis of the point of shipment. See McGunan, The New Order in Provincial Profit Allocation (1958), 6 Can. Tax J. at 150 at 151; Eaton, Provincial Profit Allocation (1958), 6 Can. Tax. J. 7. Investment income is allocated on the same basis by deleting it from both numerator the demoninator of the allocation formula.

107. See the Income Tax Regulations, S. 402(3). Part IV of the Regulations provides special rules for special industries, but it is doubtful if elaborate technical refinements are constitutionally cognizable. What would be wanted from a court test is a broad rule to define the outer limits of competence. Fine tuning of tax equities would be a task for the legislature, not for constitutional elaboration.

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destined for export, and it is clearer still that a province, by taxation of export products, cannot provide a stimulus to provincial industry. In Texada Mines v. A.G.B.C.[108] the Supreme Court struck down British Columbia legislation which imposed on iron ore mined in the province, and provided a premium for iron ore processed in British Columbia. The intent of these acts was to provide incentives for refining facilities to locate in British Columbia. They failed as export taxes.

Suppose that a province, rather than imposing taxation on export goods, provides for significant write-offs in respect of goods that are locally processed. The legislation might distinguish between different industries, or different sectors of the same industry. Would such a scheme withstand constitutional examination? Certainly the export tax theory would be highly relevant. The point to notice is that by means of a taxation scheme discrimination is made between the price of a good to be charged in the export market according to whether the good was or was not processed in the local jurisdiction. Such a scheme suffers from a second constitutional defect. It discriminates between goods in the current of interprovincial trade.

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108. Texada Mines v. A.G.B.C. [1960] S.C.R. 713.

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(iv) Relation to Federal Trade and Commerce Power

The second constitutional prohibition of substance is that provincial tax systems may not be used as impediments to the "flow" of interprovincial trade. Section 92:2 imperfectly expresses this idea by requiring the tax to be "in order to the raising of a Revenue". In Brant Dairy v. Milk Commissioners of Ontario[109] the Supreme Court made clear that the governing test respecting undue interference with federal trade and commerce by a province is an intention to restrict or control the free flow of interprovincial trade. Collateral interference with the flow is tolerable.[110]

It is extremely difficult, however, to say how far this prohibition reaches in respect of provincial taxation powers. It is clear law that a province is incompetent to legislate "in relation to" the price of an export good.[111] One is unable to say, however,

109. Brant Dairy v. Milk Commissioners of Ontario [1973] S.C.R. 131 at 165. This extends to import goods as well as export goods: see A.G. Manitoba v. Manitoba Egg and Poultry Association [1971] S.C.R. 689.

110. Carnation Co. Ltd. v. Que. Agricultural Marketing Bd. [1968] S.C.R. 238.

111. A.G. Manitoba v. A.G. Canada [1925] A.C. 561; CIGOL v. Sask., supra. There is no objection, however, to a provincial scheme fixing maximum and minimum prices for goods sold within the Province even if the goods originated outside the Province. Home Oil v. A.G.B.C. [1940] S.C.R. 444. This case can only be rationalized as a case dealing with a good which has left the "flow" of interprovincial trade.

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when taxing legislation is "in relation to" price. In this respect the Supreme Court of Canada appears to regard as insufficient, to support provincial taxing competence, evidence of the fact that a commodity is sold in the market at prevailing market prices.(112)

The second difficulty encountered in appreciating the prohibition against interference, by means of taxation, with goods in the flow of interprovincial trade is the uncertainty of current law on the federal trade and commerce power. It is by no means clear when a good enters or leaves the stream of interprovincial trade marking the start or finish of the exportation process.(113) The clearest statement of law on this point is by Laskin J., who, in

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112. CIGOL v. Sask. supra. The majority's reasoning has been heavily criticized in the popular press. Claude Ryan refers to it as "Un jugement inquietant et dangereux"; Le Devoir, Nov. 29, 1977, p. 4. An editorial in Le Droit (Nov. 30, 1977) refers to it as "de l'huile sur le feu". "As great a blow to confederation as any cultural outrage one could imagine being perpetuated on Quebec" reports the Montreal Star, Dec. 10, 1977, p. 13-5. The Financial Post suggests "The Supreme Court appears to be swinging one way while popular sentiment is swinging the other;" Dec. 10, 1977, p. 7.

113. Compare Home Oil v. A.G.B.C. [1940] S.C.R. 444; Carnation Co. Ltd. v. Que. Agri. Mk. Bd. [1968] S.C.R. 238; A.G. Manitoba v. Manitoba Egg and Poultry Assn. [1971] S.C.R. 689; Brant Dairy v. Milk Comm. of Ont. [1973] S.C.R. 131; Burns Foods v. A.G. Manitoba [1975] 1 S.C.R. 494; Macdonald v. Vapor Canada (1976), 7 N.R. 477 (S.C.C.).

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the Manitoba Egg Reference,[114] expressed the view that a good did not leave the export stream upon entry into the province where it was destined to be sold, but only when it had passed to the retailer for distribution to the consumer.

In the United States the Courts conceive of a "process of exportation" whereby goods are carried out of the territorial limits and severed from the mass of property domestically held. There must be an intention of uniting the goods to the mass of things belonging to a foreign country.[115] The process of exportation is narrowly conceived. Goods do not cease to be part of the general domestic mass until they are shipped or entered with a common carrier for the purpose of transportation to a foreign state. It is not enough that there be an intention or plan of exportation, or an integrated series of actions which will end with export to mark the entry of a good into the export stream. In Empresa Siderugica v. Merced[116] a cement factory was sold to a Columbian corporation. Title passed and possession was taken by the purchaser. An export license was obtained pursuant to which twelve percent of the plant was shipped. A tax levied by a municipality at that point was upheld by the U.S. Supreme

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114. A.G. Manitoba v. Manitoba Egg and Poultry Assn. [1971] S.C.R. 689 at 714.

115. U.S. v. Hill 34 F. (2d) 133.

116. Empressa Siderugica v. Merced 337 U.S. 154

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Court on the theory that the remaining portion of the factory might still have been diverted into the domestic market.

(v) Conclusions

To my mind, the best way to deal with these problems is to widen simultaneously federal jurisdiction over the export streams and provincial powers of collateral indirect taxation. The process of exportation ought to be robustly conceived. A good ought be held to enter the export stream when it is produced with the intention that it is destined for the export market, and acts are done in furtherance of that intention which leave no uncertainty in the mind of the court that the good is actually destined for export. Receipt into the foreign jurisdiction where the good is destined for consumption may be a premature point at which to mark exit from the export stream. Such an early exit would allow a province to discriminate between provincially produced goods and extra-provincially produced goods. The prevention of such discrimination is the chief advantage to be gained by delaying exit from the export stream until delivery to the retailer for sale to the consumer.

This broad conception of the reach of the export stream has the advantage of preventing a province from sending its imposts abroad through the exportation current to Canadians generally. However, in my view, in tandem with this schematic of the export stream, provincial powers of collateral indirect taxation ought to be simultaneously flattered. No province ought find itself

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embarrassed for want of compliance with purely formal requirements when those formal requirements have ceased to serve any known constitutional value. Finally, clear evidence of actual interference with the export stream ought to be mandatory. The court presumes that the legislatures have acted constitutionally.[117] Mere speculation that there is interference with price, or with the level of trade flow is not enough. Actual interference ought need to be affirmatively established by him attacking provincial competence.

(7) Death Taxes

The provinces have a wide latitude in imposing death taxes. A province may tax (1) any beneficiary domiciled or resident within its borders, (2) all or any of the testator's property situate in the province at his death, (3) any transactions that occur within the province by reason of death. If the tax is a personal tax, as long as it falls directly on persons domiciled or resident within the province, there can be no objections taken that the measure of the tax has reference to property located both within and without the province.

There are two limitations. A province may not impose

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117. Kruger and Manuel v. The Queen (1977), 75 D.L.R. (3d) 434 at 439 (S.C.C.)

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upon non-residents in respect of property located outside of the province (whether or not the deceased was resident within the province). Additionally, a province cannot impose on a domestically located executor in the expectation he will recoup from extra-provincial beneficiaries.

The substantive rule is that a province must limit itself to imposing death taxes within the province (on persons, property or transactions), but the substantive rule often finds expression in a formal requirement that the tax be direct within the meaning of Mill's test. Thus, in Provincial Treasurer of Alta. v. Kerr[118] the Privy Council made it clear that the executor could not be used as a conduit to reach extra-provincial beneficiaries, although there would be not objection to a requirement that the executor be used as a gathering point for collection of tax imposed on domestic citizens. The same point earlier had been made by the Privy Council in Cotton v. The King.[119] This case concerned a Quebec tax on all moveable property, wherever situated, of a testator domiciled in the province. Lord Moulton, in considering whether the tax was direct, said this:

> "Take, for instance, the case of moveables such as lands or shares in New York bequeathed to some person not domiciled within the province... How then would the Provincial Government obtain

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118. Provincial Trea. of Alta. v. Kerr [1933] A.C. 710.

119. Cotton v. The King [1914] A.C. 176.

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> the payment of the succession duty? It could only be from someone who was not intended himself to bear the burden but to be recouped by someone else [the notary]. Such an impost appears to their Lordships plainly to lie outside the definition of direct taxation..." (120)

The point to notice is that Lord Moulton considered the crucial example to be an impost which fell on extra-provincial citizens. This was expressed in the language of direct and indirect taxation. In my submission this analysis goes too far. Can there be any worthwhile objection to this form of tax if the tax is confined within the provincial borders, although it be framed substantially as an indirect tax? My view is that there is no reasonable objection. Accordingly, I would suggest that the measure of a province's collateral indirect taxation power, in respect of succession duties, be taken to be any taxation short of that which traverses the provincial border and imposes on citizens outside of the provincial jurisdiction. The form of the tax could be a tax on the executor, although the only safe course for a draftsman to follow is a tax on the beneficiaries with the executor used as a collection agent.

These rules can require rather gymnastic feats of legislative drafting. The Nova Scotia Succession Duty Act (121) provides as follows:

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120. Id. at 195.

121. The Succession Duty Act S.N.S. 1972, c. 17.

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"8(1) Subject as hereafter otherwise provided, duty shall be paid on all property of a deceased that is situated at the time of the death of the deceased, within the Province.
(2) Subject as hereafter otherwise provided, where property of a deceased was situated outside the Province, at the time of the death a deceased and the successor to any of the property of the deceased was a resident at the time of the death of the deceased, duty shall be paid by the successor in respect of the property to which he is the successor.
2.(5) Where a corporation which is not a resident of the Province, other than a corporation without share capital, by reason of the death of a deceased acquires or becomes beneficially entitled to property of the deceased;
(a) The corporation shall be deemed not to be the successor of the property except to the extent that the value of the shares of the shareholders of the corporation is not increased in value by the corporation acquiring or becoming beneficially entitled to the property; and
(b) Each of the shareholders of the corporation shall be deemed to be a successor of the property of the deceased to the extent of the amount by which the value of his shares in the corporation is increased by the corporation acquiring or becoming beneficially entitled to the property."

These provisions were considered in Cowan v. Minister of Finance of Nova Scotia.[122] In that case the deceased transferred considerable assets to an Alberta corporation in exchange for shares and a promissory note. By his will the shares and note were bequeathed to executors to pay income to a second Alberta corporation,

122. Cowan v. Minister of Finance [1977] C.T.C. 230.

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whose shares were beneficially owned by a third Alberta corporation, whose shares were owned by his wife. On the death of the wife, the securities were to be divided into four parts; one part was to be transferred to a daughter resident in the U.S., and the three remaining parts to be distributed to three Alberta companies whose shares were owned by three of the testator's daughters resident in Nova Scotia. Counsel for the estate attacked s. 2(5) of the Act on the ground that it was an attempt to tax property not situate within the province. That attack failed. Mr. Justice Hartt relied on the Supreme Court's decision in Kerr v. Superintendent of Income Tax[123] as explained by Mr. Justice Freedman in C.P.R. v. Prov. Treasurer of Manitoba.[124] In the latter case Mr. Justice Freedman said this:

> "A Province may directly tax any person found within its borders. It is not disputed that the appellant is carrying on business in Manitoba in such a way as to make it amenable to provincial taxation. In imposing a direct tax on such a person, it is competent for the Province to measure same by income derived both from within and from without the province; Kerr v. Superintendent of Income Tax (1942), 4 D.L.R. 289. If, however, the tax is not a tax on a person, but is rather a tax on specific property or income apart from the person,

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123. Kerr v. Superintendent of Income Tax [1942] S.C.R. 435.

124. C.P.R. v. Provincial Treasurer of Manitoba [1953] 4 D.L.R. 233.

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such property or income must be within the province. (ibid.)"

Mr. Justice Hartt considered that s. 2(5) of the Nova Scotia Succession Duty Act was valid to the extent that the shareholders benefited were residents of Nova Scotia. He added that the province would not have power to tax non-resident shareholders of these corporation, but only those who are resident successors under subsec. 8(2) of the Act.

It is clear that the province must be astute not to fall afoul of the formal direct taxation requirement. Where the province merely seeks to reach persons, property, or transactions situate within the province, its collateral powers to do this indirectly may be considerable, but they should be relied on only by hard pressed counsel supporting existing legislation, and certainly not by any draftsman. However, when the province seeks to reach property or persons outside its borders, the formal requirement of directness becomes a requirement of substance, and the province's ancillary indirect taxing powers are minute. This raises rather subtle problems where incorporeal property is concerned. Mr. LaForest noted this in 1967:(125)

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125. G.V. LaForest, The Allocation of Taxing Power Under the Canadian Constitution (1967), pp. 93-4. The leading Privy Council decisions respecting situs of intangibles for succession duty purposes are summarized at p. 94 ff.

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> "It seems reasonably clear that the same property may for constitutional purposes have a different situs for various types of taxes and thus infuse into the phrase "within the Province" a chameleon-like character. Still the law has known more curious animals, and what one is really concerned with is the proper allocation of taxing power among the provinces."

Mr. La Forest, as I understand him, is of the opinion that, in approaching these matters, the court should consider itself to be an outgrowth of the Department of Regional Economic Expansion. His view is that the poorer provinces pay a disproportionate share of the burden of customs tariff. "To redress the balance there should, it is suggested, be a general judicial policy favouring the location of property in the poorer provinces".(126)

The courts have generally declined the invitation to act as branch offices of DREE. In Re Wolfenden Estate(127) the British Columbia Supreme Court re-affirmed that it is necessary to determine the situs of incorporeal property by the applicable common law rules. The court held, further, a provincial legislature was incompetent to prescribe the conditions fixing situs of the shares for death tax purposes.

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126. Id., p. 96.

127. Re Wolfenden Estate [1971] 5 W.W.R. 108, affd. sub. nom. First Nat'l Bank of Nevada and Minister of Finance (1972), 28 D.L.R. (3d) 756.

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What are the applicable common law rules to determine situs of intangibles? Generally speaking, the theory relied on by the courts is the "power theory". This involves a judicial determination of in what jurisdiction the intangibles most effectively can be dealt with. In Brassard v. Smith[128] Lord Dunedin adopted the words of Duff J.:

> "And the chief baron's judgment, I think, points to the essential element in determining situs in the case of intangible chattels for the purpose of probate jurisdiction as 'the circumstance that the subject in question could be effectively dealt with in the jurisdiction.' This is, in their Lordships' opinion, the true test, where could the shares be effectively dealt with?"

In The King v. National Trust Co.[129] the Supreme Court of Canada laid down three principles which have been widely followed and which form a constitutional limitation to provincial ability to levy succession duties. They are:

(1) Intangible property can have but one local situation for the purpose of determining the incidence of a provincial tax upon property transmitted by reason of death.

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128. Brassard v. Smith [1925] A.C. 371

129. The King v. National Trust Co. [1933] S.C.R. 670.

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(2) The local situation of intangible property must be determined by the application of common law principles for the purpose of provincial taxation.

(3) A provincial legislature cannot increase its taxing powers by altering common law rules for determining the situs of intangibles.

The Wolfenden case concerned an amendment to the Companies Act of British Columbia. By that amendment the transfer of a share or other interest of a deceased member in a company made by his personal representative could be effected only by being made on a register specified at Section 82. Section 82 provided that the principal register of the company be located in B.C. The Act, therefore, had the effect of locating the situs of the shares in the province of B.C. according to the "power theory". Mr. Justice Hinkson held the amendment to the Companies Act a colourable attempt, under the guise of company law, to alter the situs of shares in order to bring the situs within the province, and therefore invalid.

There is something in Mr. La Forest's criticism that the common law rules respecting situs of intangibles are arbitrary and uncertain. How, after all, does one settle constitutional jurisdiction over a mortgage secured by New York lands, owed by a Quebec debtor to an Ontario testator whose executor is located

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in Alberta, and whose beneficiaries are scattered across the U.S. and Canada? But there is nothing in Mr. La Forest's solution. It is inappropriate. Nothing could be more unseemly, or engender more suspicion, than a New Brunswick court, in a dispute involving New Brunswick and Ontario, appropriating to the New Brunswick jurisdiction succession duty revenues on the "have not theory". A court cannot take on such a blatant political function, absent clear legislative direction. Further, in my view, legislative direction to this end is not appropriate. Regional equalization is not, nor could it effectively be, a judicial task; it is, and ought to remain, a legislative and administrative task.

(8) Provincial Marketing Imposts

The Provinces were obstructed early in their efforts to regulate marketing of agricultural goods by means of compulsory pooling. Provincial competence to impose a self financing mandatory pool was first doubted in Lawson v. Interior Tree Fruit and Vegetables Committee.[130] Mr. Justice Duff held the imposition of levies and license fees "for the purpose of defraying the expenses of the operation"[131] incompetent to British Columbia in the

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130. Lawson v. Interior Tree Fruit and Vegetable Committee [1931] S.C.R. 357.

131. Produce Marketing Act S.B.C. 1926-7, c. 54, s. 10(k).

following terms:

> "I think moreover, that Levies of that character, assuming for the moment they come under the head of taxation, are of the nature of those taxes on commodities which have always been regarded as indirect taxes. If they are taxes, they cannot be justified as direct taxation within the province. That they are taxes, I have no doubt."(132)

In Lower Mainland Dairy Products Sales Adjustment Committee v. Crystal Dairy Limited(133) the Privy Council considered a provincial scheme whose object and purpose was to regulate the marketing of manufactured and fluid milk. The market was congested; producers for the fluid milk market received substantially higher returns than producers for the manufactured milk market. The scheme contemplated equalizing the positions of producers for the manufactured and fluid markets, and to this effect levied an adjustment impost. Ancillary to this import was an expenses levy designed to defray the cost of the marketing scheme. The Privy Council, in a heavily critized judgment,(134) struck down the entire scheme as indirect taxation incompetent to the Province. A majority of the

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132. Lawson v. Interior Tree Fruit and Vegetable Committee [1931] S.C.R. 357 at 362-3.

133. Lower Mainland Dairy Products Sales Adjustment Committee v. Crystal Dairy Ltd. [1933] A.C. 168.

134. Laskin, Provincial Marketing Levies: Indirect Taxation and Federal Power (1959-60), 13 U. of Tor. L.J. 1.

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Supreme Court of Canada in Reference Re the Farm Products Marketing Act specifically approved the Crystal Dairy doctrine respecting equalization levies in holding that the imposition of fees by Ontario to pay for losses in marketing the surplus of a regulated product, and the use of those fees to equalize return to producers, was ultra vires as being an indirect tax.(135)

There are three significant objections to the mode of analysis employed by these cases. First, the cases offer no criteria whatsoever by which to distinguish taxes and service charges(136) although it is hard to see that expenses levies are other than service charges incident to a regulatory scheme. Second, the cases fail to distinguish regulation, by means of compulsory pooling of products or returns, from taxation. In a pooling scheme, compulsory levies never reach provincial coffers for general revenue purposes; they are returned to the producers rateably. In taxation the levies fall into the general provincial fund to be used for general provincial purposes.(137) Third, the analysis is entirely unsubtle in

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135. Reference re The Farm Products Marketing Act [1957] S.C.R. 198. The Crystal Dairy case was accepted also, albeit without examination, in Lower Mainland Dairy Products Board v. Turner's Dairy Ltd. [1941] S.C.R. 573 and P.E.I. Potato Marketing Board v. Willis [1952] 2 S.C.R. 392.

136. See La Forest, supra., at 49.

137. See generally, Laskin, Provincial Marketing Levies: Indirect Taxation and Federal Power, supra.

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distinguishing legislation imposing taxation (assuming the levies to be taxation) ancillary to an otherwise valid regulatory scheme, and legislation "in relation to" taxation. In other words, the cases seem to assume that there is no collateral power of indirect taxation in the provinces.

These are compelling criticisms, and largely through their force the Crystal Dairy doctrine was attenuated by subsequent cases. In 1938 the Privy Council, in Shannon v. Lower Mainland Dairy Products Board,[138] had occasion to consider a provincial marketing scheme which did not contain adjustment levies as a feature designed to equalize the returns to producers, but which did contain an expenses levy to defray the cost of the scheme. The expenses levy was held valid as an incidental feature to legislation otherwise valid under Sections 92:9, 92:12 and 92:16. This case dealt a death blow to any suggestion that the Crystal Dairy doctrine extends to other than an equalization levy.

The doctrine, in respect of equalization levies, has met with a similar fate, despite its brief reaffirmation in

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138. Shannon v. Lower Mainland Dairy Products Board [1938] A.C. 708.

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Reference re Farm Products Marketing Act.[139] In Crawford and Hillside Farm Dairy Limited v. Attorney General of Canada[140] the Supreme Court considered a pooling arrangement for producers of milk, whereby all milk produced was sold to a provincial board. A feature of the arrangement was that the more lucrative fluid milk market was allocated among producers. The proceeds from the pool market were then rateably distributed to producers. The substantial producers of fluid milk received a distribution based only on their allotment for production of fluid milk as fixed by the board. That lowered their returns, but left in the total pool a higher value for rateable distribution to other producers. It was in effect an equalizing scheme having the intention to equalize production returns to all producers in British Columbia, despite differences in production for the manufactured or the fluid milk market. The Court held the scheme valid as regulation in relation to Sec. 92.16 of the B.N.A. Act.

A similar scheme was considered by the Ontario High Court and Ontario Court of Appeal in Ex parte Channel Islands Breeds

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139. Reference re The Farm Products Marketing Act [1957] S.C.R. 198.

140. Crawford and Hillside Farm Dairy Ltd. v. A.G.B.C. [1960] S.C.R. 346.

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Milk Producers Association[141]. That case concerned comprehensive provincial regulation by a pooling scheme under the Milk Act[142] which created one pool for all milk produced within Ontario. An order of the Milk Marketing Board, which established one class of milk only, was attacked as ultra vires by the Channel Island Producers in that it failed to distinguish their milk from other classes of milk in the pool. Milk produced from Channel Island cows is more suitable than standard breed milk for the lucrative fluid milk market. It was said that the establishment of one pool for both industrial and fluid milk and the payment to all producers, by the board, of one blended price for their milk regardless of the type, was a compulsory taking of a portion of the returns properly due to the Channel Islands producers for the purposes of subsidizing the standard producers. In effect, it was an equalization scheme similar to the Crawford Dairy scheme. Counsel for the Commission submitted, first, that the Crystal Dairy and Turner's Dairy cases were overruled by the Reference re Farm Products Marketing Act and Crawford decisions. As a second point it was said that there was no material difference between the facts of the Crawford case and those of the

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141. R. v. Ontario Milk Marketing Bd. Ex Parte Channel Islands Breeds Milk Producers Association (1969), 2 O.R. 121, affirming (1969), 2 D.L.R. (3d) 346.

142. The Milk Act S.O. 1965, c. 72 as amended by the Milk Amendment Act S.O. 1967, c. 53.

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Channel Islands Producers case. The court agreed that the Crawford case and the Channel Islands Producers case were indistinguishable, and upheld the scheme on that ground. The High Court made obiter remarks as to the continuing life of the Crystal Dairy doctrine as follows:

> "I do feel constrained to remark, however, that the result in the Crawford case, is, to my mind, totally incompatable with the Crystal Dairy decision. Both schemes involved an equalization of returns to all producers, regardless of the end usage of their milk. In addition, in the Crawford case, there was a further equalization of returns to the vendors. I note that I am reinforced in my opinion herein by the remarks of Laskin J.A. at pp. 724-8 of his text, Canadian Constitutional Law, 3d Edition, 1966."

Kelly, J.A., speaking for the unanimous Court of Appeal, said this:

> "We agree that the statement of Rand J. in the Farm Products Marketing Act case, supra, to the effect that any element of indirect taxation is purely incidental to the major feature of control and regulation of marketing and is not a disqualifying factor is applicable to the facts of the instant case."

A case of considerable interest in this respect is the decision of the Manitoba Court of Appeal in Gershman Produce Company Ltd. v. Manitoba Marketing Bd.(143) This was an attack on the Natural Products Marketing Act, 1964 as amended by S.M. 1965, c. 57, S.M. 1966-67 c. 43, and Regulations thereunder (Reg. 106/68,

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143. Gershman Produce Co. Ltd. v. Manitoba Marketing Board [1971] 4 W.W.R. 50.

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135/68). By these acts a compulsory pooling system was established for producers of Manitoba potatos. By s. 10 of Order No. 1/68 of Manitoba Reg. 135/68 "commission serviyes charges to potato producers unless otherwise provided herein shall be 15 cents per 75 lbs.". The court rejected the attack based on indirect taxation. The court noted that since Reference re Farm Products Marketing Act, 1957, "there can be no doubt it is intra-vires a provincial legislature to authorize a marketing commission to impose fees on producers to cover service charges."

The Gershman case bears a considerable similarity to P.E.I. Potato Marketing Board v. H.B. Willis Inc.(144) In the latter case an order of the appellant board imposed on every dealer a levy at the rate of one cent for each 100 lbs. of potatoes shipped or exported by such dealer from the island. Order No. 6 of the Board repealed Order No. 2 "subject to the provision that every dealer shall continue liable to pay to the board the full amount of the charge or levy which is not due..." Mr. Justice Kerwin, with whom Fauteux J. concurred, struck down these orders as matters in relation to export trade. Mr. Justice Tashereau held the orders invalid both as matters in relation to export trade and as indirect taxation. He said, at p. 411: "The effect of this charge or levy

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144. P.E.I. Potato Marketing Board v. Willis [1952] 2 S.C.R. 392.

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necessarily tends to increase the sale price by the amount of the tax." Mr. Justice Rand held the scheme invalid as one of export trade regulation. Mr. Justice Estey held the scheme invalid as a commodity tax which was indirect.

The Manitoba Court of Appeal did not say why the levies in the Gershman case are distinguishable from Willis. One supposes that they are distinguishable as expense levies which are, since the Shannon case in 1938, supportable. Yet it is instructive to note that the Willis impost was 1 cent per 100 lbs. The Gershman impost was 15 cents per 75 lbs. One would have thought that if the Willis impost was impeachable as a commodity tax the same could be said of the Gershman impost. To the extent that the Gershman impost is referable to the expenses of the compulsory marketing scheme, it is, of course, distinguishable. However, one cannot help but remark that the administration of the Gershman scheme either must have been extremely expensive, or else the legislator was attempting to collect behind the shield of expenses levies. Whatever the case may be it is clear that a measure of indirect taxation was tolerated by the Manitoba Court of Appeal in the Gershman case. It would seem excessive formality to distinguish the cases by saying that Willis involved a levy upon a dealer, while Gershman concerned a levy upon a producer. One would have thought that the ultimate burden was borne by the extra-provincial consumer in either case.

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In the writer's submission, the Gershman case ought to be read as another touchstone in the growing list of cases which allows the provincial legislatures collaterally to levy indirect taxation to some extent. Gershman would appear to go the furthest as the indirect taxation there intrudes across the provincial border. It is an ancillary levy on producers who produce goods in the course of inter-provincial trade.

I have previously argued that when, by any regulatory scheme, taxation travels across a provincial border, the province's power of collateral indirect taxation is minute. That such holds true despite the Gershman case is made clear in P.E.I. Potato Marketing Board v. Sunny Isle Farms Ltd.(145) In this case Mr. Chief Justice Campbell considered a fee payable to the Potato Board pursuant to s. 4 of Order A-1/1963 of the Board. This was a levy of 1¢ per cubic weight of all potatoes shipped from Prince Edward Island. Mr. Chief Justice Campbell held this invalid as being in the nature of an indirect tax. His reasoning is based upon the theory that the levy would be passed back by the paying dealer to his vendor, and ultimately to the producer in the way of a reduction in the purchase price per cwt. The reasoning is suspect but not the

145. P.E.I. Potato Marketing Board v. Sunny Isle Farms Ltd. (1969) 7 D.L.R. (3d) 263.

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result. It seems that the real reason such a levy is invidious is because it brings into provincial coffers moneys coming from the pockets of extra provincial citizens. The indirect feature of the levy cannot be gotten round on the distinction between consumer and commodity taxes because the consumer, in this case, is outside of the provincial territory. In the writer's submission, the province is disentitled, except to a very marginal extent, if at all, to attract extra-provincial revenues from extra-provincial citizens by means of taxation or regulatory schemes that impose fees in excess of the expenses of the regulation.

The cases just discussed clearly shrank the Crystal Dairy doctrine beyond recognition; the recent Reference re Agricultural Products Marketing Act[146] dealt a death blow to whatever remained. The Reference involved consideration, inter alia of S. 2(2) of the Agricultural Products Marketing Act[147] which section empowered the Governor in Council, by order, to authorize provincial boards to impose expenses and adjustment levies in respect of agricultural products in both intraprovincial [S. 2(2)(a)] and interprovincial

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146. Reference re Agricultural Products Marketing Act, (1978) 19 N.R. 361 (S.C.C.).

147. Agricultural Products Marketing Act R.S.C. 1970, c. A-7.

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[S. 2(2)(b)] trade. The court was unanimous that marketing levies, whether expenses or equalization levies, are not taxes and expressly overuled the Crystal Dairy case. Mr. Chief Justice Laskin said this:

> "...it is, in my opinion, a mistaken view to regard the various types of levies associated with marketing schemes as species of taxes; they are integral to the operation of the schemes and are, in the context thereof, related either to their administration or price mechanisms designed to make the schemes tolerable and equitable for those compulsorily brought within their ambit. This view is at variance with what was said by the Privy Council in the Crystal Dairy case, but that case was itself reduced by later cases and, in my opinion, ought no longer to be regarded as stating the law on the subject of marketing levies."(148)

Without the support of the federal indirect taxing power - the levies were held to be regulatory measures; not taxes - S. 2(2)(a) of the Agricultural Products Marketing Act authorizing the levies in respect of intra-provincial trade had no constitutional foundation. It was a direct invasion of provincial jurisdiction over intra provincial trade and therefore ultra vires. But it is instructive to note that even had S. 2(2)(a) been able to gather strength from the federal taxing power by judicial refusal to overule the Crystal Dairy case, the section still would have been constitutionally defective. It is clear law that the federal taxing power can never be used to finance a regulatory scheme which, standing alone, is beyond federal

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148. Reference re Agricultural Products Marketing Act, supra, p. 33.

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competence.[149] Mr. Chief Justice Laskin re-emphasized that point in his consideration of S. 2(2)(a).[150]

The breadth of the ruling in Reference re Agricultural Products Marketing Act should not be overestimated. Adjustment or equalization levies of the kind considered in the case are not "in order to the raising of a Revenue;" they do not enhance the provincial treasury. The levies are destined for rateable distribution to producers; they do not reach, nor are they intended to reach, provincial coffers. That is principally the reason why it is artificial to regard them as taxes. Suppose, therefore, that incidental to a provincial marketing scheme, levies, in excess of expenses engendered by the regulation, were imposed without any intention of ultimate return to the producers' pool; they were brought directly into the provincial consolidated revenue fund. Does the post Crystal Dairy case law or the Agricultural Products Marketing Act Reference lend constitutional support to such an imposition? In my submission, they do not, and, absent independent constitutional grounding in the provincial catalogue of powers - as if the levies otherwise bear a rational functional connection to the marketing scheme - the imposts would fall as indirect taxation.

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149. In Re Insurance Act of Canada [1932] A.C. 41 at 52; Reference re Employment and Social Insurance Act [1937] A.C. 355 at 356; Readers Digest Assn. v. A.G. Canada (1966), 66 D.T.C. 5073 at 5075 (Que. Q.B.)

150. Reference re Agricultural Products Marketing Act, supra p. 32.

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## B. THE PROVINCIAL LICENSING POWER

### (1) Difficulties of Relating Secs. 92:2 & 92:9

The provincial legislatures have a second source of revenue raising competence. It is the licensing power found at S. 92:9 of the B.N.A. Act. S. 92:9 provides that:

> "In each Province the Legislature may exclusively make Laws in relations to Matters coming within the Classes of Subject next hereinafter enumerated; that is to say: -
>
> 9. Shop, Saloon, Tavern, Auctioneer, and other Licenses in order to the raising of a revenue for Provincial, Local or Municipal Purposes."

The clause has been a source of difficulty. A plain reading of the text appears to confer a species of taxing power in respect of the enumerated categories of business. Prima facie, the clause contemplates indirect taxing power as the fees will be passed on as part of a higher price for goods and services. There are two difficulties in the way of this reading: (1) The Privy Council has concluded that there is no genus between the enumerated businesses; the words "other licenses", thus, are unrestricted.(151) (2) The Privy Council has found the source of provincial trade regulatory power elsewhere than in Section 92:9; it has said, moreover, that S. 92:9 cannot constitute a source of such power.(152)

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151. Brewers and Malsters' Association v. Ontario [1897] A.C. 321; Lawson v. Interior Tree Fruit and Vegetable Committee [1931] 2 D.L.R. 198.

152. Lawson v. Interior Tree Fruit and Vegetable Committee [1931] 2 D.L.R. 193.

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If the first point means that the provinces are competent to indirectly tax any type of business by means of a licensing scheme, section 92:2 is rendered substantially nugatory. If the provinces are limited to direct license fees as part of a licensing scheme, then Section 92:9 has no independent force. Its revenue raising powers would be subsumed totally within S. 92:2, and the courts hold that it confers no autonomous regulatory power either.

A possible way over these difficulties is the suggestion that any fees levied by a province, pursuant to a licensing scheme, must be limited in amount to the expenses of the scheme. In other words, the provinces are competent to regulate pursuant to heads of Section 92 other than head 9; head 9 allows the costs of regulation to be defrayed by means of license fees. According to this line of argument, the provinces are incompetent to go further and levy license fees in excess of regulatory costs.

Insofar as the object of this suggestion is to revivify section 92:9 as a meaningful source of power, it is of dubious assistance. The Privy Council has found the source of regulatory power, in respect of local businesses, in sections 92:13 and 92:16. Since 1938,[153] moreover, the power to impose expenses levies for

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153. Shannon v. Lower Mainland Dairy Products Board [1938] A.C. 708.

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for such schemes has been found in those sections as well. It has been unnecessary to resort to Section 92:9 to do these things. The difficulty, therefore, remains one of logic. Either S. 92:2 is substantially rendered meaningless, or S. 92:9 is substantially rendered meaningless.

(2) Sec. 92:9: How Far a Source of Indirect Taxing Power?

The first comprehensive treatment of this problem was by Duff J. in Lawson v. Interior Tree Fruit and Vegetable Committee.(154) Mr. Justice Duff agreed with earlier authorities that S. 92:9 was not a separate source of regulatory power. He said this:

> "On the other hand, the last mentioned head authorizes licenses for the purpose of raising a revenue and does not, I think, contemplate licenses which in their primary function, are instrumentalities for the control of trade- even local or provincial trade."

Mr. Justice Duff considered that any provincial regulatory source of power must be found within other heads of s. 92; for example s. 92:8, s. 92:10, s. 92:13, or s. 92:16. S. 92:9 could not of itself constitute a source of regulatory power.

Did Mr. Justice Duff then consider that s. 92:9 had no independent force? That proposition certainly does not emerge from his reasons. He considered that levies incidental to an otherwise

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154. Lawson v. Interior Tree Fruit & Vegetable Committee [1931] 2 D.L.R. 193.

valid provincial regulatory scheme could be imposed in the form of license fees and that such levies need not meet the test of directness required by s. 92:2. He said this:

> "Prima facie it would appear, from inspection of the language of the two several heads [s. 92:2 and s. 92:9], that the taxes contemplated by No. 9 are not confined to taxes of the same character as those authorized by No. 2 and that accordingly imposts which would properly be classed under the general description 'indirect taxation' are not for that reason alone excluded from those which may be exacted under head 9." (155)

It might of course be said that this explanation of Mr. Justice Duff's words is no explanation at all. The point could be taken that Mr. Justice Duff was contemplating only an expenses levy to defray the administrative costs of an otherwise valid regulatory scheme. That may be so, but it must be recognized that Mr. Justice Duff was writing in 1931 before it was clear law that an expenses levy was valid. Indeed, two years later, the Privy Council struck down an expenses levy which was incidental to an equalization scheme. (156)

In 1938 the Privy Council made it clear in Shannon's case (157) that an expenses levy was valid. But their Lordships

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155. Lawson v. Interior Tree Fruit & Vegetable Committee [1931] 2 D.L.R. 193 at 198.

156. Lower Mainland Dairy Product Sales Adjustment Board v. Crystal Dairy [1933] A.C. 168.

157. Shannon v. Lower Mainland Dairy Product Board [1938] A.C. 708, 4 D.L.R. 81.

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appear to have extended the words of Mr. Justice Duff. Lord Atkin said this, at 86:

> "On this part of the case their Lordships, with great respect, think that the present Chief Justice, then Duff J., took a somewhat narrow view of the provincial powers under s. 92:9 in Lawson v. Interior Tree Fruit and Vegetable Committee, where he says, 'on the other hand, the last mentioned head authorizes licenses for the purpose of raising revenue, and does not, I think, contemplate licenses which in their primary function, are instrumentalities for the control of trade - even local or provincial trade.' It cannot as their Lordships think, be an objection to a license plus a fee that it is directed both to the regulation of trade and to the provision of revenue. It would be difficult in the case of saloon and tavern licenses to say that the regulation of the trade was not at least as important as the provision of revenue. And if licenses for the specified trades are valid, their Lordships see no reasons why the words 'other licenses' should not be sufficient to support the enactment in question."

I say that this is an extension of Mr. Justice Duff's words, but it may be argued that their Lordships, in Shannon's case, are in fact extending Lawson's case only by constituting s. 92:9 as a separate source of provincial regulatory power and not be extending provincial taxing competence. That argument presents this difficulty: if s. 92:9 is a separate source of regulatory power, the provincial legislatures would have easy access to otherwise exclusively federal fields. If this conclusion be not admitted, then I fail to see any distinction between s. 92:9 and the source of provincial regulatory power flowing from Secs. 92:8, 10, 13 and 16.

I would offer another interpretation of Shannon's case.

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My view is that Lord Atkin, in holding Mr. Justice Duff took a narrow view, was pointing to the narrowness, pursuant to s. 92:9, of restricting the provinces to the imposition of an expenses levy only. Lord Atkin went further. He held, as I understand him, that s. 92:9 was a source of revenue raising power for the provinces not restricted to the expenses of a regulatory scheme. The section could constitute a source of indirect taxation power ancillary of an otherwise valid regulatory scheme.(158)

If this interpretation be right, the crucial question which remains in the wake of Shannon is this: how far does s. 92:9 allow the provinces to go in levying, incidental to an otherwise valid regulatory scheme, indirect taxation for the raising of a revenue for provincial purposes? In other words, the essential question at the present day is, to what extent does s. 92:9 constitute an exception to s. 92:2?

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158. It follows from this interpretation that I am in disagreement with the views of Mr. La Forest, who says: "Section 92:9 is left with virtually no independent force of its own;" The Allocation of Taxing Power under the Canadian Constitution (1967), p. 135. I believe that this view is untenable from the vantage point of the cases discussed by Mr. La Forest, but particularly so from the perspective of cases decided subsequent to the writing of his dissertation. See my discussion of these infra.

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When a province undertakes to regulate a trade pursuant to a valid source of provincial power, it may impose indirect taxes against that trade in the form of license fees. But there is a caveat. The whole legislative scheme must be in relation to the regulation of a trade pursuant to some source of legislative power other than s. 92:9 of the B.N.A. Act. It must not be in relation to the raising of monies by indirect taxation. In sum, my submission, resting on Shannon and later cases, is that s. 92:9 constitutes an independent source of provincial collateral indirect taxation power when used ancillary to a valid regulatory scheme.

It may be argued that the recent interpretation of the provinces' taxation powers has granted such a collateral indirect taxation power without recourse to s. 92:9. Even if true, the extent of the judicially created power, as well as the extent of s. 92:9, remain uncertain. In any event, that the courts should have judicially created such a power does not mean that s. 92:9 is not independently a constitutional source of that power. The argument does not follow that because the courts have created a provincial power of collateral indirect taxation, s. 92:9, interpreted as a source of such a power, is thereby rendered meaningless.

This view of s. 92:9 means that the provinces have a power of collateral indirect taxation power greater than anything hitherto recognized by legal writers or the courts. To take an

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example: Suppose that ancillary to an equalization scheme like that considered in Reference re Agricultural Products Marketing Act[159] levies are imposed beyond the expenses of the scheme and beyond that which is rateably returned to producers. Are such levies valid? As noted above, the Reference Re Agricultural Products Marketing Act itself is not of sufficient amplitude to support the levies. However, Section 92:9, on this view, will support them. There is one requirement. The levies must be truely ancillary to the scheme. By ancillary, I mean that they must bear a rational functional connection[160] to it. If they do, then no constitutional objection fairly ought to lie to the levies being brought into the general revenues of the province for use for general provincial purposes.

(3) Recent Consideration

The major question which remains, following Shannon's case, is how far a province may go in imposing collateral indirect taxation, in the form of license fees, pursuant to s. 92:9. There are recent cases which consider the scope of power thereby granted.

The amplitude of the licensing power was considered by the Supreme Court of Canada in Reference re The Farm Products

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159. Reference re Agricultural Products Marketing Act S.C.C. Jan. 19, 1978.

160. Papp v. Papp [1970] 1 O.R. 331 per Laskin J.A.

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Marketing Act, Ontario[161] but no clear majority view is expressed in the judgments of the Court. The reference concerned the validity of certain licensing provisions respecting the marketing of hogs, peaches, and vegetables. Mr. Justice Rand, in considering the validity of the license fees, said this, at 219:

> "The language of Lord Atkin [in Shannon's case] seems to involve the conclusion that fees incidental to Provincial regulation of trade by license are to be considered without reference to the restriction of s. 92:2; and this appears to have been the opinion of Duff J. in Lawson... The power to regulate embraces incidental powers necessary to its effective exercise; and the exaction of fees to meet the expenses of such administration as that of the schemes, regardless of their incidence, is within that necessity."

Mr. Justice Locke similarly restricted himself to holding that the license fees could be justified as expenses levies. He said this, at 236:

> "The power vested in the Province to legislate in relation to licenses in order to the raising of a revenue for provincial, local or municipal purposes under head 9 of s. 92, in my opinion, authorizes this section [s. 2 of Reg. 145/54], even though their imposition in an amount which varies with the quantity sold, may tend to increase the sale price. It must, I think, be taken as decided by the judgment of the Judicial Committee in Shannon's case that it is not a valid objection to a license, plus a fee, that it is directed both to the regulation of trade and to the provision of revenue. While the functions of the marketing board and grower's committee are not defined in the material,

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161. Reference re The Farm Products Marketing Act, Ontario [1957] S.C.R. 198.

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> it is proper to assume, in my opinion, that these license fees are to defray the expenses of these bodies in discharging their duties under the scheme. The fact that the license fee may be charged in respect of peaches processed for export does not, in my opinion, invalidate the section."

Fauteux J. also considered that the license fees need not meet the test of direct taxation but he limited himself to expressing an opinion on their validity as expenses levies.

In Nelson v. City of Dartmouth(162) an attack was made against a municipal by-law imposing a license fee of $15.00 per month on operators of mobile home parks for each mobile home situate in the mobile home park. The by-law was attacked as ultra-vires in that it overstepped the limits of s. 92:9. Counsel argued that the legislation was enacted for the colourable purpose of imposing a personal property tax upon the owners of mobile homes situate in the parks in question. Mr. Justice MacDonald, in considering this submission, held as follows:

> "In my view, a genuine licensing-tax provision imposed for the primary purpose of revenue or for revenue purposes incidental to valid provincial regulation of such an operation as that of mobile home parks - as is the case here - is not invalidated by the circumstance that the tax may be indirect in its general incidence: Reference re Farm Products Marketing Act."

There is no requirement in this case that the indirect taxation by way of license fee be limited to the expenses of the regulatory

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162. Nelson v. City of Dartmouth (1964), 45 D.L.R. (2d) 183.

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scheme, nor is there any indication that the fees were so limited. The only limitation referred to by the Court is that the license fees must be in relation to the regulation of mobile home parks and not in relation to the raising of revenue by indirect taxation.

Some further light is thrown on this question by the judgment of the Supreme Court of Canada in Lieberman v. The Queen(163) This case concerns a St. John by-law to regulate and license pool halls and bowling alleys in the City. All keepers of pool halls and bowling alleys, as a condition precedent to operation, were required to obtain licenses at specified fees. Any person who failed to comply with any of the provisions of the by-law was penalized by a fine of $20.00 for each contravention. Mr. Justice Ritchie upheld the by-law as in pith and substance in relation to the regulation of hours at which businesses of special classes shall close in a particular locality. He went on to note that such is merely a private matter in the province. In so holding, Mr. Justice Ritchie said this, at 131:

> "Nor do I think it can be said that S. 3 of the by-law is inoperative as being in conflict with the Lords Day Act. The licensing power vested in the provinces by S. 92:9 is not limited to the shop, saloon, tavern and auctioneer licenses specified in that section, and if that power is exercised in respect of a merely local matter and in a manner which is not repugnant to Federal or provincial law, the provincial authority is, in my opinion, entitled to attach such conditions

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163. Leiberman v. The Queen [1963] S.C.R. 643.

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> and impose such penalties as it may see fit in respect to the manner in which the person so licensed shall conduct the businesses which are the subject of such licenses."

The point to notice is the lack of requirement that the fees and penalties do not exceed the expenses of the regulatory scheme.

This problem has received recent consideration in Lafarge Concrete Ltd. v. District of Coquitlam [164] and clear support for the line of argument I have followed has thereby emerged. The municipality of Coquitlam, which is well favoured with abundant supplies of sand and gravel, undertook to regulate the removal of such gravel by by-law No. 1489 in 1967. The by-law was a complete code of regulation providing for safety and environmental control. A license fee of $50.00 per year was imposed. This was amended by by-law 2041 in 1971. By by-law 2041 the permit fee was varied from a flat annual charge to one of fifteen cents per cubic yard of soil removed. This came to approximately 10% of the average selling price of the gravel removed and sold by the respondent. The amending by-law was unsuccessfully attacked before the British Columbia Court of Appeal as indirect taxation incompetent to the province or its derivative municipalities.

Mr. Justice Taggart upheld the amending by-law on the

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164. Re Lafarge Concrete Ltd. v. District of Coquitlam (1973), 32 D.L.R. (3d) 459 (B.C.C.A.)

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basis that its governing intention was to defray "the costs incurred and to be incurred by the appellant municipality in constructing and maintaining roads giving access to the gravel pits and the cost of supervising, inspecting and enforcing the by-law". That, essentially, treats the fees as expenses levies. However, the majority of the court was not so restrictive. Mr. Justice Bull considered that indirectness in any impost which did not fall within S. 92:2 "may still be within the scope of provincial competency if contemplated by and fairly authorized under another head such as here - Sec. 92:9." He continued, at 464:

> "In my view, the key lies in the question as to what is the primary and real purpose, or pith and substance, of the legislation - is the levy or tax (whether direct or indirect by nature) merely ancillary, or adhesive, to the licensing scheme of regulating or prohibiting a trade or is it essentially a fiscal imposition, or taxation, under form of disguise or a colourable concept?"

Mr. Justice Branca was similarily expansive in his consideration of the authorities. He declined to limit himself to the proposition that S. 92:9 could impose indirect taxation ancillary to a valid regulatory scheme only to the extent of defraying the expenses of that scheme.

The Lafarge case is of some considerable interest. It indicates that the key test is not whether the quantum of indirectness extends beyond the actual expenses of a regulatory scheme. It holds that the test, rather, is whether the indirect imposts are truly ancillary; in which case they are valid. If, on the contrary,

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they are a colourable attempt to legislate in relation to indirect taxation, then the legislature has exceeded its powers. The distinction is fine, but it is very real, and in my submission it must now be taken to be Canadian law.

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## IV. VACUUMS IN THE TAXING POWER

### (1) Section 121

One of the grand aims of Confederation was the creation of a single economic unit in which the diverse regional economic potentials of the new state would dovetail into complementary strength. S. 121 expressed this idea by making provision for free trade throughout the confederated union. The section, in terms, holds incompetent to any authority interference with the free admission of goods into a province.

It is important to notice that Sec. 121, in terms, offers incomplete protection of the Canadian common market. It applies only to "articles of growth, produce, or manufacture". It does not apply services; it does not apply to labour; it does not apply to capital; it does not apply to incorporeal property such as goodwill or information. Furthermore, the test of Sec. 121 refers to "entry". It does not apply to exit. Perhaps, in domestic commerce, entry into one province implies exit from another. But in the case of international trade goods may exit from a province without making entry into any other province, and without, in express terms, coming within the ambit of Sec. 121 protections.

The permeability of Sec. 121 to provincial taxation is problematic. To take the paradigm situation: Suppose that in consequence of provincial language policies a steady current of businesses move their operations out of the Province of Quebec.

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The Province responds by placing restrictions on capital leaving the province. In the case of business liquidations it enacts a direct tax which is 50% of the liquidation value in the case where the capital is pre-intended to exit from Quebec. It is arguable - but only arguable - that such a tax falls afoul of the prohibitions on the provinces not to interfere with citizenship (165) interprovincial trade,(166) or to levy export taxes.(167) But if these attacks fail, does Sec. 121 offer any more likely prospect of success?

In the first half of this century, Sec. 121 was very narrowly construed by the courts. In Gold Seal v. Dominion Express Mr. Justice Duff stated that "the real object of the clause is to prohibit the establishment of customs duties affecting interprovincial trade in the products of any province of the Union."(168) That statement of the reach of Sec. 121 has been approved by the Privy Council(169) and widely followed.

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165. Union Colliery v. Bryden [1899] A.C. 580, as explained in Cunningham v. Tomey Homma [1903] A.C. 151.

166. Carnation Co. v. Quebec Agricultural Marketing Board [1968] S.C.R. 238 (Provinces must not exhibit an intention to control interprovincial trade).

167. Texada Mines v. A.G.B.C. [1960] S.C.R. 713.

168. Gold Seal v. Dominion Express (1921), 62 S.C.R. 424.

169. Atlantic Smoke Shops v. Conlon [1943] A.C. 550

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Recent judicial consideration of Sec. 121 indicates that it may serve as an important constitutional plank in the regulation of interprovincial streams of commerce. This suggestion was made by Mr. Justice Rand, who, in considering the word "free" in the clause, expressed the view that "'free' in Sec. 121, means without impediment related to the traversing of a provincial boundary." He continued: (170)

> "I take Sec. 121, apart from Customs duties, to be aimed against trade regulation which is designed to place fetters upon or raise impediments to or otherwise restrict or limit the free flow of commerce across the Dominion as if provincial boundaries did not exist. That it does not create a level of trade activity divested of all regulation I have no doubt; what is preserved is a free flow of trade regulated in subsidiary features which are or have come to be looked upon as incidents of trade. What is forbidden is a trade regulation that in essence and purpose is related to a provincial boundary."

This view was echoed by the Manitoba Court of Appeal in Reference re Interprovincial Trade Restriction on Agricultural Commodities(171). The court found legislation establishing a

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170. Murphy v. C.P.R. (1959), 15 D.L.R. (2d) 145 at 150, 153.

171. Reference re Interprovincial Trade Restrictions on Agricultural Commodities (1971), 18 D.L.R. (3d) 326; aff'd. sub nom. A.G. Manitoba v. Manitoba Egg and Poultry Assn. [1971] S.C.R. 689.

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comprehensive regulating scheme for eggs invalid because it had the "effect of impeding the free flow of trade between provinces and therefore runs counter to Sec. 121 of the B.N.A. Act."

This view was approved, on appeal to the Supreme Court, by Mr. Justice Laskin, who put the point in this way:

> "The Manitoba scheme cannot be considered in isolation from similar schemes in other provinces; and to permit each province to seek its own advantage, so to speak, through a figuative sealing of its borders to entry of goods from others would be to deny one of the objects of confederation, evidenced by the catalogue of federal powers and by Sec. 121, namely, to form an economic union of the whole of Canada: see the Lawson case." (172)

The Chief Justice gave further consideration to the substance of Sec. 121 in Reference re Agricultural Products Marketing Act. Counsel in that case objected to a surplus disposal feature of the egg marketing regulation; it was said that S. 23(1)(a) of the Farm Products Marketing Agencies Act 19-20-21 Eliz. II, c. 65, which established a quota system for the marketing of eggs in interprovincial trade, effectively prevented the establishment of a single economic unit in Canada with absolute freedom of trade between its constituent parts contrary to what was provided for in Sec. 121. Mr. Justice Pigeon, speaking for the majority of the court, expressed the view that quotas at the stage of production, which distinguish goods destined for intraprovincial trade from those destined for

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172. A.G. Manitoba v. Manitoba Egg and Poultry Assn. [1971] S.C.R. 689 at 717.

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interprovincial trade, are not competent to the Dominion. Mr. Justice Pigeon did not refer to Sec. 121, but the Chief Justice, who disagreed on this point, did so expressly in these words:

> "It seems to me, however, that the application of S. 121 may be different according to whether it is provincial or federal legislation that is involved because what may amount to a tariff or customs duty under a provincial regulatory statute may not have that character at all under a federal regulatory statute. It must be remembered too that the federal trade and commerce power also operates as a brake on provincial legislation which may seek to protect its producers or manufacturers against entry of goods from other provinces."

> "A federal regulatory statute which does not directly impose a customs charge but through a price-fixing scheme, designed to stabilize the marketing of products in interprovincial trade, seeks through quotas, paying due regard to provincial reduction experience, to establish orderly marketing in such trade cannot, in my opinion, be in violation of Sec. 121."

There follows a cite from Murphy after which the Chief Justice continues:

> "Excepting this view of Sec. 121 I find nothing in the marketing scheme here that, as a trade regulation, is in its essence and purpose related to a provincial boundary. To hold otherwise would mean that a federal marketing statute, referrable to interprovincial trade, could not validly take into account patterns of productions in the various provinces in attempting to establish an equitable basis for the flow of trade. I find here no design of punitive regulation directed against or in favour of any province." (173)

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173. Reference re Agricultural Products Marketing Act, (1978) 19 N.R. 261 (S.C.C.).

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That these cases expand the reach of Sec. 121 is incontrovertible, but it is idle speculation to inquire how far Sec. 121 currently extends, in respect of taxing legislation, without relating the section to the entire corpus of law on trade and commerce. Sec. 121, in its revivified form, offers textual authority for holding safe from interference currents of interprovincial trade. Taxing legislation which has the effect of impeding those currents - currents identified by recent considerations of the trade and commerce power - might well fall afoul of Sec. 121. In principle, this result could follow whether the legislation was enacted by Parliament pursuant to Secs. 91(2) and 91(3) or by a provincial legislature pursuant to Sec. 92(2) (174)

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174. Federal incompetence, by virtue of S. 121, to levy a tax in respect of interprovincial goods was referred to by Mr. Justice Dubin in dissenting reasons in Reference re Agricultural Products Marketing Act, Ont. C.A., Jan. 10, 1977. He said this:

> "It it conceded that Parliament can impose a tax on all egg producers in Canada, but if it chooses to do so, in my respectful opinion, it should be done in the manner contemplated by the British North America Act with the safeguards therein provided. In the instant case, power is given to a provincial agency to impose what is said to be a tax apparently for the purpose of pooling amongst the producers of eggs engaged in the intraprovincial market of the monies realized from the sale of their product. To uphold the validity of such legislation raises implications which, in my opinion, transcend the matters brought in issue by this Reference. Can Parliament in purporting to regulate export trade give a provincial agency authority to impose an export tax on goods across provincial boundaries which would appear to be inconsistent with s. 121 of the British North America Act."

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However, the Murphy case makes plain that Sec. 121 does not hold interprovincial currents of trade safe from interference in any free market, or laissez faire sense. Canada's federal and provincial governments are not prohibited from regulating such trade so as to achieve an efficient allocation of resources; Sec. 121 offers no impediment per se to state interference in the economy. Any argument to this effect is very wide of the mark. What the section does inhibit is trade regulation serving only to reinforce purely provincial objectives.(175) The question, which remains open in the case law, is which provincial objectives? It is clear that Sec. 121 makes incompetent legislation which protects the provincial market by taxing goods entering that market. Can it protect the provincial market for services by taxing services seeking to enter? Information? Goodwill? If the answer to these questions is negative, then the Canadian common market is incompletely realized.

(2) Section 125: Intergovernmental Immunity

Section 125 establishes an immunity from taxation for federal and provincial lands and property. There can be little

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175. See the highly illuminating remarks of Safarian, Canadian Federalism and Economic Integration (Ottawa: Information Canada, 1974), p. 58

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doubt that the guiding spirit behind the section was the prevention of any disturbance being caused to the federal union by a misuse of taxing powers.(176)

The framers of the constitution could not have foreseen the enormous commercial undertakings engaged in by all levels of government. Such activity raises questions as to how far Sec. 125 presently reaches. If, for example, the province of Ontario were to acquire Place Ville Marie, would it do so immune from Montreal tax assessments?(177) Can Alberta's ownership of Pacific Western Airlines be enjoyed free from all tax liability?(178)

The first distinction which suggests itself is a distinction between taxation of lands and property and taxation of occupiers or users of lands and property. A tax against the property is bad,(179) but a personal tax against an occupier of property suffers from no infirmity.(180) In principle, there

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176. A.G.B.C. v. A.G. Canada (1922), 64 S.C.R. 377 at 385.

177. See Laskin, Canadian Constitutional Law, p. 758.

178. See the Income Tax Act S. 149(1)(d) which hold immune from tax liability corporations which are at least 90% owned by a domestic government. This Section, of course, is not constitutionally obligatory.

179. Stinson v. Middleton Township (1949) 2 D.L.R. 238.

180. Sammartino v. A.G.B.C. [1972] 1 W.W.R. 24.

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ought to be no objection, if the tax is a personal tax, to the fact that the measure of the tax has reference to the value of the property.

There is a second distinction of importance. Section 125 prohibits only taxation against crown property; it does not prohibit charges for services rendered. If the service charge is truely other than taxation, no claim of incompetence to impose it ought to succeed because the amount of the charge is based on the value of crown property. Neither should there be merit in a complaint as to mode of exigibility. However, great care must be taken in drafting a statute imposing compulsory charges for services, as an involuntary mode of subscription for the service might well be decisive in attracting characterization as a tax. In R. v. Breton (181) a Quebec City levy on property owners for sidewalk maintenance was held inapplicable, by reason of Sec. 125, to the Dominion government. In Société Centrale d'Hypotheques v. Cité de Québec (182) a snow removal charge was held by Montgomery J., in light of its compulsory nature, to be a tax. These cases should be contrasted with Minister of Justice v. Lévis (183) in which charges imposed

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181. R. v. Breton [1967] S.C.R. 503.

182. Société Centrale d'Hypotheques v. Cité de Québec [1961] B.R. 661.

183. Minister of Justice v. Lévis [1919] A.C. 505.

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by the City of Levis for water supplied were upheld as service charges.

Finally, it appears clear that a tax against a third party, with the expectation that the charge will be passed on to the federal or provincial Crown in the form of increased cost for services, will not attract the prohibition of Sec. 125.(184) The tax is viewed as being a tax on the third party only, and not an invidious march on governmental immunity.

(3) Taxes Collected Pursuant to an Ultra Vires Statute

If moneys are demanded and collected pursuant to a taxing statute subsequently determined by the Courts to be ultra vires, those moneys must be returned. No government can by prior or ex post facto legislation give itself competence to retain such moneys. This principle recently was stated by the Supreme Court of Canada in Amax Potash v. Government of Saskatchewan(185) as follows:

> "To allow moneys collected under compulsion, pursuant to an ultra vires statute, to be retained would be tantamount to allowing the provincial legislature to do indirectly what it could not do directly and by covert means to impose illegal burdens."

Provincial incompetence to legislate so as to retain the moneys collected follows whether the statute is ultra vires, as in Amax

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184. R. v. Bell Telephone Co. (1935), 59 B.R. 250 (Que.).

185. Amax Potash v. Government of Saskatchewan [1976] 6 W.W.R. 61 at 73 (S.C.C.)

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Potash, or inoperative for conflict with paramount federal legislation.(186)

It is a nice question as to whether this principle prohibits retention of the identical moneys by means of retroactive taxing legislation. In principle, one would have thought the answer was negative. Amax Potash prohibits retention of moneys collected by an illegal statute. The case assumes a lack of authority, constitutionally exercised, to collect the moneys. If the retroactive taxing legislation is in relation to a competent source of constitutional power, then there is no want of authority to collect the moneys. The retroactive feature makes this true ab initio. Ex hypothesi, there is constitutional power to collect the moneys; accordingly, there ought to be no complaint that the legislation does indirectly that which the province cannot do directly. The point of distinction is that by retroactive taxing legislation, the legislature is doing directly that which it can do directly, but hitherto had not done.

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186. Re The Coloured Gasoline Tax Act [1977] 4 W.W.R. 436 (B.C.S.C.).

## V. GENERAL CONCLUSIONS

The constitutional distribution of taxation powers in Canada addressed problems which have become historically obsolete. The original allocation reflected the view that the provincial legislatures were economically subordinate bodies entrusted with legislative responsibilities deemed insignificant. This has ceased to be the case entirely in fact and in theory. A review of the constitutional cases by which the provincial taxation powers were expanded in order to take account of the political reality is a history of gradual widening. This has been done by flattering provincial powers of indirect taxation, provincial powers of hybrid taxation, and, to a lesser extent, the provincial licensing power.

This case law is constructed largely upon a fictitious legal doctrine. This is the legal definition of direct taxation. That definition has become so cumbrous and difficult of application that it inevitably produced judicially erratic results, and a constitutional law unsatisfactory in principle. Yet there is, through the verbiage, a clearly discernable trend. That trend is that the limitation of provincial power to direct taxation has become largely a matter of form. The substantive limitations braking provincial taxing competence is that the provinces confine themselves to taxing "within the province" by enacting taxation which, economically speaking, produces effects limited to the provincial territory. It is suggested that the fiction and

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verbiage be stripped away, and that the limitation of form, direct taxation, be seen for what it is, an archaic and outmoded political-economic doctrine which has ceased to serve any constitutional value. But at the same time, constitutional requirements of substance need to be underlined. These requirements are a prohibition on the provincial legislatures from interference with interprovincial streams of commerce, and an aroused sense of respect for the provincial border so far as concerns the economic ripples produced by provincial taxation measures.

Lastly, constitutional doctrine respecting the provincial licensing power needs to be rethought completely. This process has begun in certain recent cases, and it can be extended by reinterpretation of the old Privy Council decisions. But before the licensing power can take clear shape, it must be reemphasized that the power is subservient to demanding constitutional values. Those values are largely synthesisable from examination of what the courts have done to the provincial direct taxation power. That is, absent compelling reasons of policy, such as the necessity provincial taxation be confined to the provincial jurisdictions. a broad amplitude needs to be given to provincial capacity to finance provincial schemes. Having stripped away ancient and outmoded doctrine from the constitutional distribution of taxation powers in Canada, it is possible for jurisprudence concerning the provincial licensing power to pursue a more sensible course.

A. CASES, ACTS & STATUTES

A.G. Alberta v. A.G. Canada [Bank Taxation Reference] [1939] A.C. 117

A.G.B.C. v. A.G. Canada (1922), 64 S.C.R. 377 at 385

A.G.B.C. v. C.P.R. [1927] A.C. 934

A.G.B.C. v. Kingcome Navigation Co. [1934] A.C. 51

A.G.B.C. v. McDonald Murphy Lumber Co. [1930] A.C. 357

A.G. Canada v. A.G. Ontario [Unemployment Insurance Reference] [1937] A.C. 355

A.G. Manitoba v. A.G. Canada [1925] A.C. 561

A.G. Manitoba v. Manitoba Egg and Poultry Association [1971] S.C.R. 689

A.G. Nfld. v. The Avalon Telephone Co. Ltd. (1962), 33 D.L.R. (2d) 402

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The Agricultural Products Marketing Act R.S.C. 1970, c. A-7

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