TAXATION IN CANADA*

Canada is a federal state with a central government and ten provincial governments. In 1867 the principal colonies of the British Crown in North America joined together to form the nucleus of a new nation and the British North America Act of that year became its written constitution. This statute created a central government with certain powers while continuing the existence of political subdivisions called provinces with powers of their own.

Under the British North America Act the Parliament of Canada has the right of raising "money by any mode or system of taxation" while the provincial legislatures are restricted to "direct taxation within the Province in order to the raising of a Revenue for Provincial purposes". Thus the provinces have a right to share only in the field of direct taxation while the Federal Government is not restricted in any way in matters of taxation. The British North America Act also empowered the provincial legislatures to make laws regarding "municipal institutions in the Province". This means that the municipalities derive their incorporation with its associated powers, fiscal and otherwise, from the provincial government concerned. Thus, from a practical standpoint, municipalities are also limited to direct taxation.

A direct tax is generally recognized as one "which is demanded from the very person who it is intended or desired should pay it". In essence, this conception has limited the provincial governments to the imposition of income tax, retail sales tax, succession duties and an assortment of other direct levies. In turn, municipalities, acting under the guidance of provincial legislation, tax real estate, water consumption, places of business and in some cases retail sales. The Federal Government levies direct taxes on income, on gifts, and on the estates of deceased persons and indirect taxes such as excise taxes, excise and customs duties, and a sales tax.

The increasing use by both the federal and provincial governments of their rights in the field of direct taxation in the 1930's resulted in uneconomic duplication and some severe tax levies. Starting in 1941, a series of tax agreements between the federal and provincial governments have been entered into under which the agreeing provinces have undertaken, in return for compensation, not to use or to permit their municipalities to use certain of the direct taxes. As a result of the most recent of these agreements, all provinces except Quebec have undertaken not to impose a personal income tax for the period 1957-62 and all provinces except Ontario and Quebec have undertaken for the same period not to impose taxes on corporations or successions. Consequently, the Province of Quebec is at present the only political subdivision in Canada levying its own personal income tax and Ontario and Quebec are the only jurisdictions imposing corporation income taxes, special corporation taxes and succession duties. (See also pp. 1067-1070.)

The fact that the Provinces of Ontario and Quebec have chosen to continue to impose income taxes and succession duties has not resulted in recent years in taxpayers in those provinces bearing a substantially heavier tax load than taxpayers in other provinces. As part of the current federal-provincial arrangements, the federal income tax and estate tax are abated by certain amounts in those provinces which also impose these taxes.

Federal Taxes

Individual Income Tax

Every individual who is a resident of Canada at any time during a year is liable for the payment of income tax for that year. In addition, every individual who is employed or carries on business in this country during a year is required to pay tax on the part of his taxable income earned in Canada. Canadian taxation practice is based to a large extent on the British experience. This is reflected particularly in the fact that taxation is on the basis of residence rather than citizenship, and in the tax freedom for capital gains. The

* Prepared (in February 1961) by F. R. Irwin, Director, Taxation Division, Department of Finance, Ottawa. This article includes federal tax changes announced in the Supplementary Budget on Dec. 20, 1960, and provincial taxation *circa* April 1961; federal tax changes announced in the Budget of June 20, 1961 are outlined at p. 1051.