

Section 2.—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 to raise "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 and places of business. 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 the 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 were concluded between the federal and the provincial governments to promote the orderly imposition of direct taxes. The duration of each agreement was normally five years. Under these agreements, the participating provinces undertook, in return for compensation, not to use or permit their municipalities to use certain of the direct taxes. Under the present arrangements, the federal income tax otherwise payable in all provinces and the estate tax otherwise payable in the non-participating provinces are abated by a fixed percentage to make room for provincial levies.

The current agreement became operative on Apr. 1, 1962 and will run until Mar. 31, 1967. Basically it entails a partial federal withdrawal from the field of direct taxation and the re-entry of all provinces into the vacated area. The federal personal income tax otherwise payable on income earned in a province and on income received by a resident of a province is reduced by the following percentages: 16 p.c. in 1962; 17 p.c. in 1963; 18 p.c. in 1964; 21 p.c. in 1965;† and 24 p.c. in 1966.† In 1965 and 1966, the federal tax abatements for income earned in Quebec or received by a resident of Quebec will be 24 p.c. and 27 p.c., respectively. The additional relief of three percentage points in the case of Quebec is to allow that province to collect revenue to pay monthly allowances for students between the ages of 16 and 18. Similar allowances in the other provinces will be paid directly by the Federal Government. The special federal income tax abatements for Quebec in 1965 and 1966 have not yet been authorized by legislation. Also, the Federal Government reduces its rate of corporation income tax on taxable income of corporations earned in the provinces. The reduction is 9 p.c. of taxable income earned in any province except Quebec and 10 p.c. in Quebec; the additional 1 p.c. reduction in Quebec is to compensate for the additional tax levied by the province on corporation income to provide grants to universities. These

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† The original agreement provided for abatements of 19 p.c. in 1965 and 20 p.c. in 1966. However, following a federal-provincial conference in April 1964, the provinces were granted an additional two percentage points in 1965 and four percentage points in 1966.