

Canada's Forgotten Centennial: 100 years of income taxes in Canada

“Sir THOMAS WHITE: Next year, 1918, [Canadian corporations] will pay a heavy taxation—I think the heaviest in the world—against their profits of 1917.

Sir WILFRID LAURIER: They are lucky to be able to do it.

Sir THOMAS WHITE: I agree with my Right Hon. friend. They are fortunate to be able to do it.”¹

*Sir Thomas White (Canada's Finance Minister)
In Commons debate with the leader of the opposition,
Sir Wilfrid Laurier, summer 1917*

Canada is naturally preoccupied with commemorating its 150th anniversary in 2017, and few among us are thinking about what happened 100 years ago. When we do think about 1917, it evokes for most of us Canada's coming of age in the great World War I victory at Vimy Ridge in April of that year.

1917 was a year when most of the developed world was wondering when the war that was supposed to have had “the boys back by Christmas,” was ever going to end. We did not have to wait long for an answer.

On February 3, the United States broke diplomatic ties with Germany.

On March 15, Tsar Nicholas abdicated the Russian throne.

On April 6, the U.S. Congress voted to declare war on Germany – just three days before the Battle of Vimy Ridge began.²

On April 16, Vladimir Lenin returned to Russia from exile.

On June 26, the first American troops landed in France.

On July 6, T.E. Lawrence (of Arabia) and his forces captured the Jordanian city of Aquaba.

On July 18th, the Russian royal family was executed.³

On October 24, the Bolshevik revolution began. Two days later, the Winter Palace was occupied and on December 14, all of Russia's banks were nationalized.⁴

Back on the home front, Canada's Union Government stopped the importation and production of alcoholic beverages as a precursor to prohibition, which began in 1918.⁵ This followed Sir Wilfred Laurier's (see our \$5.00 bill) defeat on December 17.

1. <http://wartimecanada.ca/sites/default/files/documents/IncomeWarTax.1917.pdf>

2. <http://www.firstworldwar.com/timeline/1917.htm>

3. https://en.wikipedia.org/wiki/Execution_of_the_Romanov_family

4. <https://www.marxists.org/history/ussr/events/timeline/1917.htm>

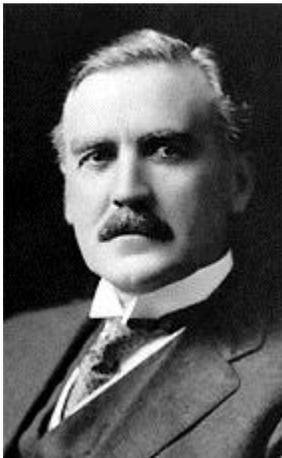
And in Ontario, a law was passed giving women the right to vote.

In other words, both in Canada and the world, major events were occurring. So perhaps we can be forgiven that another momentous 1917 event, affecting all Canadians in deeply personal and financial ways, is often forgotten:

The Borden government (see our \$100 bill) that succeeded Laurier's passed a law bringing income taxes to Canada. One hundred years later, there are no events, no stamps, no coins, no conferences, no celebrations.

The lead-up

Federal income taxation legislation came to Canada reluctantly. In 1909, the Lloyd George reformed and extended income taxes in the United Kingdom. By 1913, the US had already adopted income taxes as an answer to prohibitively high tariffs. But Sir Thomas White, who was to become finance minister under Prime Minister Robert Borden, still maintained in 1916 that "income tax should not be resorted to."⁶



Sir Thomas White

Nevertheless, Canada's war bill had climbed to over \$600 million in 1916 dollars. A variety of measures including excise taxes, import duties, and special postage stamp levies were falling catastrophically short of meeting Canada's ability to pay. Our nation was moving ever closer to even more costly conscription.⁷ And a massive loss of taxes on consumable alcohol due to Prohibition was just around the corner.

5. https://en.wikipedia.org/wiki/Prohibition_in_Canada

6. <http://www.duhaime.org/LawMuseum/CanadianLegalHistory/LawArticle-168/1917-Birth-of-Income-Tax.aspx>

7. [ibid](#)



Examples of war tax stamps with portrait of King George V: Overprints on postage and war tax stamps

The legislation

By the summer of 1917, Borden and White had changed their minds. They introduced legislation to the House of Commons on July 25:

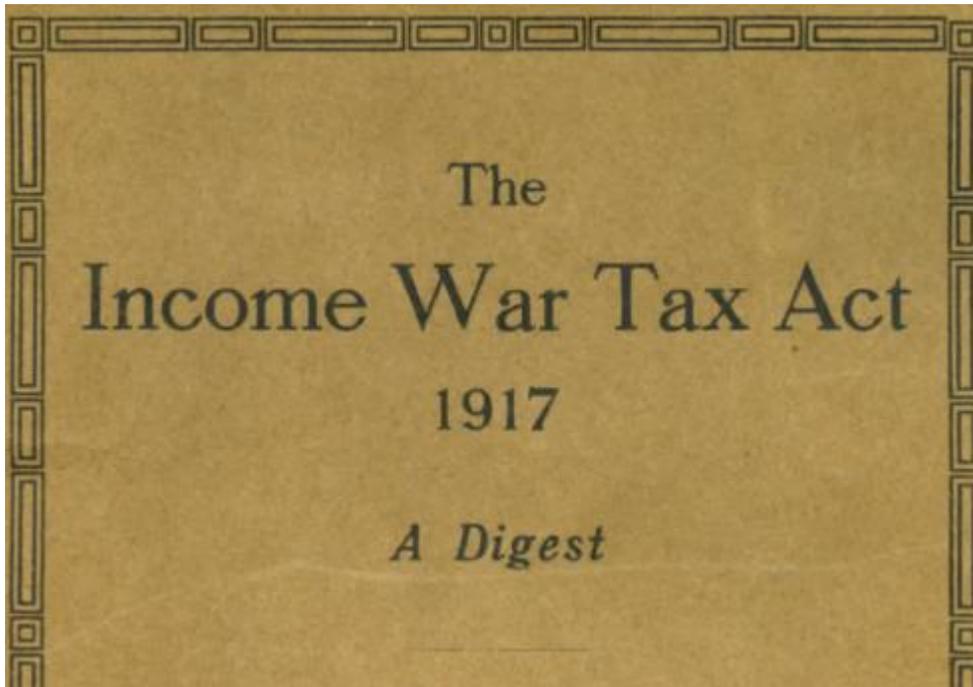
SIR THOMAS WHITE - Minister of Finance (Leeds): *Mr. Chairman, I desire today to lay before this committee, proposals for a national measure of income taxation. Hitherto we have relied upon duties of customs and of excise, postal rates and other miscellaneous sources of revenue. Canada has been, and will continue during the lifetime of those present today, to be a country inviting immigration. I have, therefore, thought it desirable that we should not be known to the outside world as a country of heavy individual taxation.*

We are, however, confronted with grave conditions arising out of the war. The time has arrived when we must resort to direct taxation. I am confident, Mr. Chairman, that the people of Canada, whose patriotism during this war has been so often and so nobly proven, will, in light of present conditions, which call for it, cheerfully accept the burden and the sacrifice of this additional taxation.

We cannot see very far ahead in these days. We do not know how long this war will last. We do not know what the attitude of the people of this country will be upon the many questions, social, industrial, financial and fiscal.

Therefore, I have placed no time limit upon this measure but merely have placed upon Hansard the suggestion that, a year or two after the war is over, the measure should be reviewed by the minister of finance of the day, with a view of judging whether it is suitable to the conditions which then prevail.

The *Income War Tax Act* passed on August 17. Canada adopted an income tax of 4% on every unmarried man for his income above \$2,000. The exemption for families was \$3,000. For incomes above \$6,000, the tax ranged from 2% to 25%. Corporations were not exempted.



Income War Tax Act 1917

The fiscal and constitutional aftermath

"I have no doubt, that once we have embarked upon it, the judgment of the country will be that it should be continued for many years to come."

—Opposition finance critic Alexander Maclean, 1917

In the blink of an eye in 1917, Canada changed in ways that took us decades to fully understand. All of a sudden, the federal government had appropriated the greatest tool available to governments to raise revenues. A permanent fiscal imbalance between the federal and provincial governments was born.

The *Constitution Act* of 1867 (originally enacted as *the British North America Act*) presented no issues. Both provincial and federal governments were given free rein to raise revenue through taxes. But the framers had no inkling in July 1867 as to what would happen almost exactly 50 years later.

Even in a cursory reading of the *Constitution Act*, the vision is clear: a highly decentralized federation where the federal government would have broad stewardship of the country through peace, order and good government, while the provinces would do the heavy lifting.

The costs of the enumerated responsibilities of the provinces in section 92 of the Act far outweigh those carried by the federal government. Sections 6, 7, 8, and 14 alone of S92 call for provincial responsibility over matters that now cost their treasuries almost 80% of the revenues they raise.

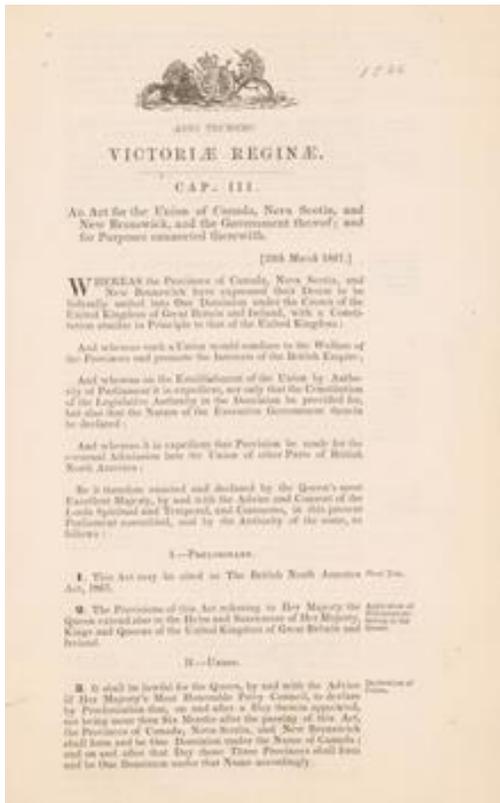
“6. The Establishment, Maintenance, and Management of Public and Reformatory Prisons in and for the Province.

7. The Establishment, Maintenance, and Management of Hospitals, Asylums, Charities, and Eleemosynary Institutions in and for the Province, other than Marine Hospitals.

8. Municipal Institutions in the Province.

14. The Administration of Justice in the Province, including the Constitution, Maintenance, and Organization of Provincial Courts, both of Civil and of Criminal Jurisdiction, and including Procedure in Civil Matters in those courts.”

–Constitution Act of Canada



First page of the BNA Act

By the 1920's, the level of government with the fewest financial responsibilities had much more money than it required, while the provinces were left with excruciating responsibilities and limited resources.

For the next 100 years, Canada's premiers were judged by their ability to squeeze revenues out of Ottawa, while prime ministers and their finance ministers were judged by their ability to close the faucets.

During the Great Depression, Ottawa ran surpluses while two provinces – Alberta and Saskatchewan – defaulted on their provincial debt. Newfoundland and Labrador, a province-to-be, also defaulted. In Ontario, many municipalities could not meet their obligations and it was not until the later 1930s that the provincial government was able to finally bail them out.

There were some constitutional amendments to redress the imbalance. The hardships of the Great Depression resulted in a 1940 amendment allowing the federal government to launch unemployment insurance. The movement to provide older Canadians with pensions led to the constitutional amendments of 1951 and 1964 to allow the federal government to levy payroll taxes, an area of provincial jurisdiction.

The courts clarified that the federal government had a new instrument called 'spending power', meaning it could spend money in areas thought to be under provincial jurisdiction. That gave us the Baby Bonus, modern Old Age Security, and eventually refundable tax credits.

But opposition leader Alexander Maclean was not so much prescient but a canny student of human nature when he predicted that Ottawa was unlikely to stop the money rolling in after repaying its war debt. Less than a decade after that was accomplished, Prime Minister Mackenzie King was openly bragging about his capacity to bully the provinces:

*"With respect to giving moneys out of the federal treasury to any Tory government in this country ... with these governments situated as they are to-day, with policies diametrically opposed to those of this government, I would not give them a five-cent piece."*⁸

–House of Commons, Debates, [April 3, 1930](#)

We are the most decentralized democracy on the planet. Few Canadians understand that the last time the federal government had a share of Gross Domestic Product that was larger than the provinces combined was 32 years ago in 1985. The federal government generates less economic wealth than the provinces collectively. Yet it levies far more income taxes in every province and territory.

8. http://canadachannel.ca/canadianbirthdays/index.php/Quotes_by_Prime_Ministers_-_Mackenzie_King

There is a general consensus that Ottawa needs to share those taxes with the provinces. But save for the crucial equalization mechanism in section 36, with its commitment to equal opportunity, our constitution – after 150 years as a nation – remains silent on how tax sharing should happen. As a result, Ottawa and the provinces are constantly squabbling over spending on things like health care without a rule book.

The only sure way to redress the fiscal imbalance between Ottawa and the provinces is to amend our constitution.

Let's celebrate our tax centennial by reopening the discussion on an amending formula we can all work with.

After Pierre Trudeau's Victoria Charter of 1970 failed to result in the adoption of an amending formula, Trudeau repatriated Canada's Constitution without Quebec as a signatory in 1981 with not one, but *five* amending formulas:

The drafters of Canada's revised Constitution created the amending formulas. They are listed in sections 38 to 49 of the Constitution Act, 1982. Creating the formulas was not easy because all of the provinces wanted to make sure they got a say if and when the Constitution was to be changed. The amending formulas are complicated. There are five different kinds of formulas. Each one is used for changing different aspects of the Constitution.⁹

Amending our Constitution is a political killing field for any issue of substance. Sure, we amended it to allow Prince Edward Island to have a fixed link to New Brunswick (PEI's ferry service was enshrined in the BNA Act). To his personal credit, Prime Minister Brian Mulroney tried twice to obtain the necessary agreement from the provinces to amend the Constitution in order to ensure a lasting place for Quebec and other distinct cultures in Canada. He failed at both Meech Lake and Charlottetown. For his trouble, Mulroney's Conservatives were reduced to a 'party of two' in the election of 1993.

No prime minister since Jean Chretien – who decreed that constitutional change was off the table – has gone anywhere near it on issues of great consequence. We won't go near it even to fix the Senate. Dare we raise the topic in the context of Canada's fiscal imbalances?

Canadians profess to pollsters that they don't like income taxes and there is at least 50 years of good evidence that they don't like constitutional change. The problem is that they also don't like the endless bickering and wrangling between the federal and provincial governments over every money issue from carbon to health, from prisons to fisheries, from income security to...on and on.

9. <https://ualawcsprod.srv.ualberta.ca/ccs/index.php/constitutional-keywords/489-amending-formula>

To change the Constitution using the general formula, the change needs to be approved by 1) the federal Parliament, 2) the Senate, and 3) a minimum number of provincial legislatures. There must be at least seven provinces that approve the change, representing at least 50% of Canada's population. This is often called the 7 + 50 rule. This means that provinces with large populations will typically need to approve a change in order for the amendment to succeed. However, the change cannot happen without some support from provinces with smaller populations.

The fact is that Canada is losing its ability to negotiate with itself. Real debates quickly degenerate into mindless squabbling about who owes who what, all the while absent the rule book that would settle the affair. Trudeau the younger's health care funding debacle is only the most recent example¹⁰.

So let's mark the second century of income taxes in Canada and celebrate the 150th anniversary of a separation of powers between provinces and the federal government in a way that befits the occasion. Let's collectively admit to the childish pickle we are in and resurrect that moribund Canadian institution, the Royal Commission.

Canada has appointed exactly 50 Royal Commissions since 1861. The last one to be appointed (on the Air India tragedy) began its work nine years ago. We have not had such a long hiatus between commissions since 1902.

We have not had a commission of inquiry into taxation at the federal level since the Carter Commission completed its work over 50 years ago in 1966. And our last shot at obtaining an amending formula that would actually work was 25 years ago in 1992.

Isn't it time for the son, Justin, to try to do what the father could not, and end the incessant wrangling about how we govern ourselves and pay for our nation?

He has already said no to that proposal but after all these years, it deserves another try.

¹⁰ In a recent Commentary for C.D. Howe, Peter Hicks make this point clear: "*Mechanisms for undertaking such detailed inter-governmental negotiations simply do not exist today. With the failure of the Meech Lake Accord in 1990 ... there is not even a set of general principles for undertaking such negotiations*".
https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_465.pdf p.7